

DRAFT ENVIRONMENTAL AND SOCIAL STRATEGY (ESS)

I. Overview

- 1.1. The objective of the Project is to increase financial access for Base of the Pyramid (BOP) public employees in Colombia by scaling up the innovative loan origination program repaid via payroll deductions (libranzas) developed by Bayport FiMSA S.A.S (“Bayport Colombia” or “BC”). BC is a non-bank financial institution focused particularly in rural areas and regions with low levels of financial inclusion and high levels of Unsatisfied Basic Needs. The use of funds will support the company’s loan origination activity and allow it to scale its existing portfolio, specifically to provide financing for home improvements, education, health, micro and small enterprises (MSEs) and agricultural activities. In order to achieve this objective, the Opportunities for the Majority Sector is proposing to provide Bayport Colombia an A/B loan of up to US\$50 MM (approx. COP\$102.6 billion) composed of an A Loan of up to US\$15 MM (COP\$31 billion) and a B Loan of up to US\$35 MM (COP\$71.6 billion).
- 1.2. BC mitigates credit risk repaid via payroll deductions based on commercial agreements with more than 360 municipalities, state institutions, and pension funds. The latter allows BC to quickly identify potential clients, assess their credit risk level and process approved loans. BC has a direct salesforce model allowing the company to actively go where its clients are based. Moreover, 80% of BC’s financing is directed at housing (home improvements), education (tuition fees and school supplies), MSEs (productive assets/working capital), agriculture (inputs and equipment), and health expenses¹. In mid-2014, BC will launch a dedicated home improvement line in alliance with specialized home improvement retailers (Corona and Home Center), and as such provide additional value added to its clients, including top quality construction materials, as well as basic technical assistance.
- 1.3. Finally, BC endorsed the Smart Campaign Principles² by applying respectful collection practices and adopting high ethical standards in the treatment of its clients.
- 1.4. Beneficiaries that wish to become eligible for the loans must meet the following requirements:
- Be formally employed by any public institution or be pensioned from one
 - Comply with credit risk requirements, including verification of over-indebtedness
 - Earn more than one monthly Minimum Wage (MW)³
 - Have a valid ID (cedula de ciudadanía)
 - Be no more than 55 and 60 years for women and men respectively for active employees
 - Be no more than 85 years for both women and men for pensioners
- 1.5. The main terms and conditions for the loans are as follows:
- Tenor between 6-60 months
 - Minimum Loan amount: COP\$1,000,000 (US\$500)
 - By law, payroll deductions cannot exceed 50% of salary after deducting other financial and non-financial obligations, such as taxes, health, social and pension benefits
 - Competitive market rates
 - Loans include a mandatory life and surety insurance

¹ The remaining 20% are mostly personal loans, which includes debt repayments/restructuring.

² The Smart campaign is based on 3 Client Protection Principles: (i) appropriate financial products to clients’ needs; (ii) FI seeks client feedback for product design and delivery; (iii) FI does not use aggressive sales techniques. www.smartcampaign.org

³ As of January 2014, the Minimum Wage in Colombia was COP\$616,000 (US\$306)

II. Environmental and Social Impacts and Risks

- 2.1 Based upon the nature of this operation consisting of financing housing (home improvements), education (tuition fees and school supplies), MSEs (productive assets/working capital), agriculture (inputs and equipment), and health expenses, there may be minimum to moderate direct environmental, social or health and safety (ESHS) and labor risks and impacts. To that end a specific environmental due diligence is required. The potential key ESHS and labor risks and impacts associated with this operation are those related to the specific goods and services financed by Bayport Colombia with the proposed financing, and could include: (i) financial, legal and reputational credit risks associated with BC's operations; and (ii) direct ESHS risks and impacts related to investments in certain sectors.
- 2.2 Financial, legal and reputational credit risks: Financial and legal credit risks refer to potential negative effects on Bayport Colombia's ability to collect on sub-loans and/or to repay the IDB because of: (i) risk of an eventual non-repayment of loan due to business interruption and environmental and social issues (e.g. liabilities, law suits, fines, etc.) associated with its loans, and (ii) risks associated with Bayport Colombia's facilities and operations, such as environmental liabilities in their offices or Bayport Colombia's employees having occupational health and safety problems due to working conditions. Reputational risks are associated with Bayport Colombia's involvement in projects, companies or activities considered unacceptable to the IDB and/or that could face significant public opposition or concerns, such as (i) inappropriate location or lack of environmental and social management of the projects; (ii) Bayport Colombia's finance application and analysis process that is not equitable, fair, and unbiased in terms of social factors (e.g. gender, age, ethnicity, or cultural heritage, etc.); and (iii) significantly deficient labor practices.
- 2.3 *Direct ESHS impacts associated with goods and services financed by Bayport Colombia:* The proposed operation may generate ESHS impacts associated with the financed loans in specific sectors. The type of impacts will vary depending on the amount of loans to be extended and on the type of activities to be financed. There may be specific impacts and risks related to investment in certain sectors, for example: Agriculture: stress on water resources, soil erosion, health problems due to pesticide use, eutrophication of aquatic environments, biodiversity impacts, crop residues and other solid waste, atmospheric emissions, physical and chemical hazards and confined space entry. Housing: The Project presents certain indirect lesser risks and impacts related to the improvement of the houses associated with: (i) the sites where the housing improvement takes place (e.g. risk of contaminated site, or natural disaster risk); (ii) the design of the housing improvement (e.g. unsafe or vulnerable structures); (iii) the housing improvement works themselves (e.g. health and safety risks to construction workers from activities associated with the use and handling of heavy equipment, air and noise pollution); (iv) the materials that will be used in construction (e.g. banned or dangerous materials)
- 2.4 These risks may be minimal to moderate and will be assessed during the due diligence.
- 2.5 *E&S Risk management capacity of the FI:* Bayport Colombia's E&S risk management capacity is estimated to be adequate given that it has dedicated environmental and social guidelines in place, and follows international best practices based on the parent company's experience (see Sponsor section in the Project Profile for further information).

III. Status and Compliance

- 3.1 Given that this is a financial intermediary operation and according to Directive B.13 of the Environment and Safeguards Compliance Policy (OP-703), this Project is not categorized.

IV. Strategy for Environmental and Social Due Diligence

- 4.1 The environmental and social due diligence for the proposed facility will verify the operation's compliance with the Bank's Environment and Safeguards Compliance Policy and guidelines. In addition, the due diligence will address those issues that are relevant to the proposed operation.
- 4.2 Therefore, the environmental and social due diligence required for this operation will comprise of the following steps:
- An assessment of BC's compliance status with the applicable environmental, social, health and safety, and labor regulatory requirements as well as with any relevant conventions and treaties which have been ratified by Colombia;
 - An assessment of BC's actual lending portfolio, to establish potential reputational risks associated with BC's involvement in projects, companies or activities considered unacceptable to the IDB;
 - An assessment of BC's existing ESMS, and its adaptability to this operation considering the amount of the loans and potential financing sectors;
 - An assessment of the capacity of current credit appraisal, approval, and monitoring procedures (exclusion list, checklists, action plans) to manage environmental and social liabilities, risks and/or impacts of SME operations.
 - An assessment of current procedures that should, at a minimum, be able to: (i) include provisions for loan officers to be trained and qualified to identify ESHS issues/liabilities; and (ii) include the consideration of environmental and social issues in the loan analysis that:
 - eliminate uses of funds which are on the IDB exclusion list;
 - filter high-risk projects that may involve potential impacts on protected areas, indigenous peoples, physical or economic displacement of vulnerable groups, possible effects that may result from natural disasters, or other significant social and environmental impacts (i.e. pollution, overexploitation of resources, impacts to health and safety of neighboring communities, etc.);
 - verify compliance of the ESHS laws applicable to sub-loans;
 - assess and manage potential risks and ESHS liabilities that may be associated with sub-loans.
 - An identification of any environmental and occupational health and safety liabilities in BC's facilities and operations and if required, an assessment of the adequacy of action plans to properly resolve them.
 - An evaluation to ensure the BC has adequate Contingency Plans and procedures (i.e. emergency response programs, building evacuation drills, etc.) including their technical competence, satisfactory level of training and sufficient resources to ensure adequate implementation.
 - An assessment of BC's procedures to ensure that loan, finance application and analysis process is still equitable, fair, and unbiased in terms of social factors (e.g. age, gender, cultural heritage, etc.).
 - Define the ESHS mitigation and management measures required for the program to meet the requirements of the Bank's safeguard policies.
- 4.3 The results of the due diligence will be presented in an Environmental and Social Management Report and summarized in the Loan Proposal to establish the environmental, social, health and safety, and labor requirements for the operation which should also be reflected in the loan agreement.