

# Technical Cooperation Document

## I. Basic Information for TC

▪ Country/Region:	COLOMBIA
▪ TC Name:	Conducive Financing Frameworks and Instruments in Sustainable Infrastructure in Colombia
▪ TC Number:	CO-T1674
▪ Team Leader/Members:	Demichelis, Jose Francisco (IFD/CMF) Team Leader; Frisari, Giovanni Leo (CSD/CCS) Alternate Team Leader; Martinez Alvarez, Juan (IFD/CMF) Alternate Team Leader; Acevedo Calle, Daniela (LEG/SGO); Hertz, Kai (ORP/GCM); Irigoyen, Jose Luis (INE/ENE); Isabella Espana Quezada (IFD/CMF); Luis Restrepo Osorio (IFD/CMF); Martinez Lopez, Cynthia (IFD/CMF)
▪ Taxonomy:	Client Support
▪ Operation Supported by the TC:	N/A
▪ Date of TC Abstract authorization:	05 May 2022.
▪ Beneficiary:	The Republic of Colombia through the Superintendency for the Financial Sector in Colombia (SFC), Financiera de Desarrollo Nacional (FDN), and the Financial Corporation for the Territorial Development (Findeter)
▪ Executing Agency and contact name:	Inter-American Development Bank
▪ Donors providing funding:	United Kingdom Sustainable Infrastructure Program(SIP)
▪ IDB Funding Requested:	US\$800,000.00
▪ Local counterpart funding, if any:	US\$0
▪ Disbursement period (which includes Execution period):	36 months (execution period: 30 months)
▪ Required start date:	July 1st, 2022
▪ Types of consultants:	Individuals; Firms
▪ Prepared by Unit:	IFD/CMF-Connectivity Markets and Finance Division
▪ Unit of Disbursement Responsibility:	IFD/CMF-Connectivity Markets and Finance Division
▪ TC included in Country Strategy (y/n):	Yes
▪ TC included in CPD (y/n):	No
▪ Alignment to the Update to the Institutional Strategy 2010-2020:	Productivity and innovation

## II. Objectives and Justification of the TC

- 2.1 **Objective.** The objective of this non- reimbursable Technical Cooperation (TC) is to foster innovation within the financial system, by supporting the National Development Banks (NDBs) and Superintendency for the Financial Sector to consolidate sustainable infrastructure finance ecosystem in Colombia. The project works on paving the way to eliminate all potential barriers that hinder bankability of a pipeline of sustainable projects. It will help to mobilize investment in infrastructure to achieve strong, inclusive, and balanced economic growth that will set Colombia on a more sustainable and inclusive development path.
- 2.2 **Background.** The Government of Colombia has invested an average of 3.6% of Gross Domestic Product (GDP) in infrastructure in recent years, nonetheless levels of around

7% per year would be required to meet growth objectives.<sup>1</sup> Infrastructure investment in the country is considered low, without action this trend will further expand. Bankability of infrastructure projects is a key issue to be addressed in the market, enhance local banks' perception of infrastructure risks can avoid high interest rates, high collateral requirements and short-term financing.<sup>2</sup> The experiences in Colombia show that public entities lack adequate mechanisms to finance projects and, in some cases, have not been able to adequately quantify the resources needed to implement infrastructure projects. To ensure the success of long terms projects, proper maturity in lending operations should be offered, in the Colombian market is not usual to find financial operations with maturities over five years, since most of the financial institutions have short term funding.

- 2.3 Colombia still has some capital market challenges due to the low number of institutional investors and initial public offerings and secondary offerings. Moreover, compared to the Organization for Economic Co-operation and Development (OECD) economies, Colombia's stock exchange is still small, and has very few listed companies compared to its regional peers. To encourage investor participation in infrastructure financing, the Government of Colombia passed a series of decrees loosening previous restrictions. In 2014, Decree 816 allowed credit institutions to invest more capital towards infrastructure, and in 2015, Decree 1385 allowed insurance companies and pension funds a similar freedom. Despite this innovation in the financial system, the sector has identified meaningful opportunities for improvement. Under the leadership of Asobancaria (union of banks in Colombia), tools are being developed to improve the assessment of environmental and social risks in lending operations.
- 2.4 Across Colombian financial sector, sustainable finance is a priority most of public and private banks have experience financing the market development and the country strategic priorities.<sup>3</sup> As a result, NDBs have robust, diverse, and healthy portfolios that make the public financial system a catalyst into the development of sustainable infrastructure. By the end of 2019, around US\$8 billion (just over 2.5% of the GDP) was the total loan portfolio under these institutions, this represents 6% of the total assets of the financial system.<sup>4</sup> The National Development Finance (FDN, by its acronym in spanish) and the Financial Corporation for the Territorial Development (Findeter) focus on infrastructure at the national level and municipalities, respectively. All the NDBs except for FDN, offer credit through second tier operations leveraging credit for the financial system, lately it is more common that NDBs to finance operations directly (especially Findeter and Bancoldex).

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<sup>1</sup> Sustainable Infrastructure Program (SIP) – baseline study, Accenture, 2019.

<sup>2</sup> There is a lack of adequate long-term financing in the financial system. The vast majority of liabilities in the sector are mainly short-term deposits (81%) where only 21% corresponds to deposits with maturities are older than 18 months (Superintendencia Financiera de Colombia, 2019). Strategies to enhance long term credit might involve the creation of long-term lending operations with NDBs in order to provide proper coupling in the credit operations.

<sup>3</sup> For example, in 2016, Bancolombia, was the first private bank in the country to issue a green bond to finance climate change mitigation projects. Another example is Suramericana an insurance company that developed with the support of Bancoldex and IDB an insurance mechanism to guarantee savings in energy efficiency projects.

<sup>4</sup> Superintendency for the Financial Sector in Colombia (SFC) – Informe de Banca de segundo piso (Instituciones Oficiales Especiales - IOE).

- 2.5 Private banks play an important role in infrastructure investments; bank commercial lending, of which infrastructure lending is a major component, represents 53% of all loans offered in the country. Also, Colombia has a healthy presence of foreign credit entities, with foreign banks accounting for 26.8% of total assets at the end of 2018 (UKSIP baseline, Accenture, 2019).
- 2.6 The role of FDN, has been instrumental in the development and growth of infrastructure financing in Colombia. FDN provides financial products through direct credit operations, securitization of assets and non-financial solutions such as project structuring, credit enhancements among others. This supplements the existing financial market with the intention of crowding-in private investors, attracting private capital at significant rates, in order to invest into transport infrastructure and energy projects recently. Findeter is oriented towards social infrastructure, has an important role in financing energy and energy efficiency projects, water, sanitation and urban development infrastructure and has been involved in several climate finance initiatives, including Nationally Appropriate Mitigation Actions (NAMAs).
- 2.7 Even though Colombia has advanced notably in sustainable finance for infrastructure, there are some key interventions that can accelerate the origination of more sustainable projects at upstream level. NDBs and the public financial system could provide a safe ground to test and implement innovative mechanisms, that can anchor the development of sustainable infrastructure. Due to the mandate of the national public banks to facilitate operations that usually are not financed by private banks, the development of such mechanisms and tools can improve the bankability of projects to leverage private investment.
- 2.8 The Superintendency for the Financial Sector in Colombia (SFC) is the public entity that ensures that the financial system is stable and contributes effectively to the progress of the country. To do so, the SFC supervises the Colombian financial system, to preserve its stability, promotes the development of the Colombian stock market and ensures the protection of investors and savers. Similarly, the SFC has focused its strategy on promoting innovation in the financial sector, as this will serve as a driver to move towards a more competitive, inclusive, and responsible financial system.
- 2.9 In compliance with its strategic objectives, during 2021 the SFC promoted new policies related to risk management, new technologies and financial system innovation, protection of the rights of financial consumers, and international standards on information disclosure for Environmental, Social and Governance (ESG) in the stock market. During 2020 decree 1393 was issued fostering the proper implementation of better risk management of investments boosting the capital market and the incorporation of ESG criteria in the investment policies of companies.
- 2.10 The Government of Colombia has made a commitment towards sustainable development during the last years, the implementation path is described by policy document of the public National Council for Economic Policy and Social (CONPES, by its acronym in Spanish).<sup>5</sup> To develop this plan the financial sector has been promoting the development of the Green Protocol through strategies to improve sustainability within the public and private banking sectors. The SFC recognizes the role of the financial system in promoting environmental and social sustainability and it seeks to

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<sup>5</sup> [Estrategia para la Implementación de los objetivos de desarrollo sostenible \(ODS\) en Colombia, CONPES 3918 - 2018.](#)

include within of the supervisor's regulatory agenda, initiatives that strengthen the practices of the financial system towards sustainable development.

- 2.11 SFC first effort to mobilize the financial sector towards sustainable development was the publication of the official position of the SFC on green finance and climate risks. In this document, plans were established on climate change and green finance agendas, including specific issues related to the inclusion of ESG criteria in investor decision making institutions. In addition, the SFC also worked on the promotion of green bonds in the private sector through the definition of the applicable regulation and taxonomy.
- 2.12 Given all the antecedents mentioned above, there is a general sector development and available financial instruments to manage climate change to some extent. Nevertheless, it includes high upfront costs, transaction costs and liquidity. the IDB has identified a comprehensive programme thought the Front-End Sustainable Low Carbon Infrastructure Analysis to address these market barriers that combines technical assistance (including at the country partnership level) with concessional financing from The Department for Business, Energy, and Industrial Strategy (BEIS) of the United Kingdom Sustainable Infrastructure Program (UKSIP) fund.
- 2.13 **Strategic Alignment.** The TC described is consistent with the Bank's Second Update of the Institutional Strategy 2020-2023 (AB-3190-2) and is aligned with development challenge of Productivity and Innovation, since it will facilitate access to financing for sustainable infrastructure, moreover the TC is aligned with IDB 2025 Vision specially in the reactivation of the productive sector objective increasing the volume of infrastructure investment and innovation. This TC will also contribute to the Corporate Results Framework 2020-2023 (GN2727-12) since it considers the value of investments in sustainable infrastructure. Also, the objective of this TC is aligned with one of the three strategic pillars of the IDB Group Country Strategy with Colombia 2019-2022 (GN-2972), to raise the quality of infrastructure and urban development, reduce transaction costs in the economy, and improve the international positioning of goods produced in Colombia. All interventions presented in document are aligned with: (i) with the needs and priorities of the Government of Colombia as well as (ii) the UKSIP funds purpose and guidelines. This TC was specially designed to mainstream sustainability across the national, sectorial, and institutional upstream level, as well as to increase institutional capacity, prioritize and build sustainable low carbon infrastructure bankable pipelines to mobilize private sector financing. The TC will help bring the SFC and the NDBs closer to international standards in terms of good practices applicable to the financial sector. All the activities of the TC will contribute to the definition of the new operating sustainability standards in the financial market. This TC will support the beneficiaries' in fulfilling the commitments acquired within the framework of the Pact for entrepreneurship, formalization and productivity, and the Pact for sustainability, National Development Plan 2018-2022 "Pact for Colombia, Pact for Equity". The TC is aligned with the National Strategy for International Cooperation in its axis of conservation and environmental sustainability. Additionally, the project is in line with the 2030 Agenda and the SDGs, particularly about SDG 9 "Industry, Innovation and Infrastructure". The TC is in line with Colombia's comprehensive policy framework towards sustainability, including a Sustainable Development Goals (SDG) National Strategy (CONPES 3918/2018) as well as a Green Growth National Policy (CONPES 3934/2018) which set up actions, goals, and indicators to increase the economic competitiveness of the country in ways that are socially, environmentally, and financially sustainable.

### III. Description of activities/components and budget

- 3.1 **Component 1. Enabling Sustainable Infrastructure ecosystem with the SFC (US\$370,000).** This intervention will further enhance the regulatory framework to leverage green capital market instruments to attract international investment to Colombia's sustainable infrastructure pipeline by providing technical assistance. Close collaboration with SFC will enhance local financiers' perception of infrastructure risks, avoiding high interest rates, high collateral requirements and short-term financing. Three activities are planned with the SFC: (i) Develop a financial facility to promote eligible issuers and loan borrowers to cover transactional costs in green/sustainable bond issuance and external review services; (ii) Strengthening capacities in climate risks in the financial sector including pension funds, financial institutions, among others; (iii) Improvement on sustainable finance taxonomy and toolkits, guidelines for KPI-linked bonds and transition bonds and capacity building.
- 3.2 **Activity 1.1.** Develop a financial facility to promote eligible issuers and loan borrowers to cover transactional costs in green and sustainable bond issuance and external review services. Under this activity, the TC will work on developing a framework to promote a facility that will enhance the capacity of investors to issue sustainable infrastructure bonds. Additional sub-activities will be planned to streamline demand and facilitate the emissions of sustainable bonds. The following sub-activities will be developed under this item: (i) comparative analysis of international experiences on issuance of sustainable bonds; (ii) detailed assessment on green/sustainable bond market challenges; analysis of legal, financial, and institutional barriers faced by potential investors; (iii) viability analysis to structure a facility that promotes green infrastructure bond issuance; and (iv) operating manual of the facility that describes the decision making, eligibility rules, disbursement process, verification, and monitoring. Under this activity the following products are expected: viability study of the facility, proposal for facility design and operating manual, outreach, and dissemination event with market actors.
- 3.3 **Activity 1.2.** Strengthening capacities in climate risks in the financial sector including pension funds, insurance companies, among others. Under this activity the TC will work on developing capacities of the market, previous experiences have been developed with banks and insurances companies however, this activity will focus on unattended market like the pension funds/investment funds. The following sub-activities will be implemented under this activity: (i) develop a training program for pension and investment funds and (ii) develop toolkits/instruments and specific material for the Colombian market relevant to investors.
- 3.4 **Activity 1.3.** Improvement on sustainable finance taxonomy and toolkits, guidelines for KPI-linked bonds and transition bonds and capacity building. Under this activity the following specific action will be held Assessment of risk differential between taxonomy compliant portfolios of the historical of Non-Performing Loans (NPL) vs business as usual portfolio and analysis of Green/Brown differential in infrastructure sector. For this activity specific training material will be developed to use the taxonomy developed by the SFC to report on the alignment, reporting and disclosure; a pilot project will be developed with at least two financial institutions. The selection criteria for this pilot will consider: the relevance of infrastructure in the total loan portfolio and available metrics in green tagged loans and investment portfolios.
- 3.5 **Component 2. Direct support to NDBs with Findeter and FDN to foster innovation in sustainable infrastructure (US\$400,000).** This intervention will support sustainable infrastructure pilots in key projects which will generate credibility and trust in the markets to achieve better replicability and scale. The objective of this

component is the generation of new lending processes, methodologies for credit assessment and technical assistance are needed to promote crucial interventions in NDBs.

- 3.6 **Activity 2.1.** Develop financial support and facilities to finance key projects related to sustainable infrastructure with FDN and Findeter. In this intervention NDBs will develop at least two pilots related to facilitate the creation of sustainable projects. The following sub-activities will be developed under this item: (i) develop “Credit factory” schemes in NDBs to accelerate the lending process for sustainable infrastructure projects; (ii) support capacity enhancement in NDBs, special efforts will be held to attract private investments in sustainable infrastructure projects, with key innovations in the market such as: securitization and bond issuance with private players, municipalities and regional governments; and (iii) training and capacity building in NDBs to enhance sustainable infrastructure access to finance.
- 3.7 **Activity 2.2.** Designing green financial instruments and products with NDBs will improve the leverage private investment for sustainable infrastructure projects in Colombia, as well as the incorporation of climate related risk mitigation measures to also mitigate financial risks (e.g., guarantees, insurance and credit enhancement). This intervention will provide cross-sectoral benefits for the private and public sector. The following sub-activities will be developed under this item: (i) identify of potential financial arrangements to attract private investments and finance (risk sharing mechanisms, project finance structuring, special purpose vehicles, syndication, dedicated long-term finance solutions); (ii) identify innovative instruments to reduce government and financiers’ exposure to foreign exchange risk (e.g., improving liquidity of long currency swaps, hedging mechanisms); (iii) enhance capacity of financial Institutions, capital markets and private banks in structuring green and sustainable bonds, by identifying, selecting and managing eligible pipeline of eligible projects; and (iv) develop evidence of ESG & climate risk management in improving the project credit risk profile.
- 3.8 **Component 3. Project Management and Evaluation (US\$30,000).** For the adequate development of the TC components, an external consultant will be hired to support: (i) the coordination of tasks with the beneficiaries; (ii) review and improvement of terms of reference; (iii) review of products to be developed in the TC; and (iv) monitoring of the indicators in the Results Matrix. This component also considers the final evaluation of the project that will be carried by an external consultant to the program.
- 3.9 **Expected results.** The TC is aimed to ensure that the SFC, FDN and Findeter develop market instruments to consolidate sustainable infrastructure market, under the described components special efforts will tackle key market barriers faced by investors and improve bankability of sustainable infrastructure projects in Colombia. The expected results of the TC are of special relevance given the infrastructure gap and the market barriers faced by investors to develop low carbon infrastructure.
- 3.10 **Budget.** The total cost of the TC will be US\$800,000 and financed by UKSIP. The donor’s contribution will finance the hiring of consulting services from firms and/or individual consultants, according to the indicative budget in Table 1 and the Procurement Plan.

**Table 1. Indicative Budget (US\$)**

Activity/Component	Description	IDB/ UK-SIP	Total Funding
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<b>Component 1</b>	<u>Enabling Sustainable Infrastructure ecosystem with the SFC</u> <ul style="list-style-type: none"> <li>- Develop a financial facility</li> <li>- Strengthening capacities regarding climate risks in the financial sector</li> <li>- Improvement of sustainable finance taxonomy</li> </ul>	250,000  50,000  70,000	<b>370,000</b>
<b>Component 2</b>	<u>Direct support to NDBs with Findeter and FDN to foster innovation in sustainable infrastructure</u> <ul style="list-style-type: none"> <li>- Develop financial support and facilities to finance key projects</li> <li>- Design green financial instruments and products with NDBs</li> </ul>	200,000  200,000	<b>400,000</b>
<b>Componente 3</b>	Project Management and Evaluation <ul style="list-style-type: none"> <li>- Monitoring and evaluation</li> <li>- Final evaluation of the program</li> </ul>	20,000 10,000	<b>30,000</b>
<b>TOTAL</b>		<b>800,000</b>	<b>800,000</b>

3.10 **Monitoring.** The Bank, through the Connectivity, Markets and Finance Division (IFD/CMF), will be responsible for the supervision and monitoring of the TC program, the Team Leader, a senior specialist (IFD/CMF), is responsible for TC execution. For the proper development of the planned activities, CMF will have an internal dedicated project team for the preparation of terms of reference, monitoring of activities, deliverable review, and logistic support, among other tasks. Annually, the project team will prepare progress reports for the indicators of this TC (see Annex II. Results Matrix), including a description of the progress made, the results obtained, the status of execution of the planned activities and suggestions for adjustments to the remaining execution period. The final evaluation of the project will be conducted by an external consultant, in accordance with Bank policies and procedures once all activities have been executed.

#### IV. Executing agency and execution structure

- 4.1 The Bank will be the executing agency of the TC through the Connectivity Markets and Finance Division (IFD/CMF). Likewise, the Bank will execute the activities in coordination and with the support from the corresponding public sector institutions such as SFC, Findeter and FDN.
- 4.2 The IDB team will consist of a team of three IFD/CMF staff members who will lead the implementation of the project. Additionally, the IFD/CMF team will be accompanied by a group of consultants. The Bank will coordinate and engage with the main stakeholders from the beginning of the implementation of the TC, seeking feedback and regularly presenting and discussing progress reports.
- 4.3 The Bank is considered to have adequate systems to guarantee the proper execution of the operation and ensure the sustainability of the implementation of the project in line with Annex 2 of "Operational Guidelines for Technical Cooperation Products" (OP-619-4). The beneficiaries have requested that the Bank execute the TC. The Bank

has the required experience in executing TC from the donor and the technical capacity to duly and timely execute the activities from this TC.

- 4.4 **Procurement.** The Bank will hire individual consultants and consulting firms, in accordance with current Bank procurement policies and procedures. All activities to be executed under this TC have been included in the Procurement Plan (Annex IV) and will be contracted in accordance with Bank policies as follows: (a) AM-650 for Individual consultants; (b) GN-2765-4 and Guidelines OP-1155-4 for Consulting Firms for services of an intellectual nature and; (c) GN-2303-28 for logistics and other related services. Acquisitions must be reflected and carried out based on the provisions of the Procurement Plan. The disbursement period will be executed in 36 months after approval.

## **V. Major issues**

- 5.1 The overall project risk is low to medium considering the longstanding record of accomplishment of the beneficiaries' previous positive experience with the IDB. The main risk in the TC is the potential delay arising from the coordination with multiple stakeholders. This risk will be mitigated by involving each counterpart focal point, that shall be designated to coordinate the development of the TC components. Focal points will be seeking feedback and regularly presenting and discussing progress reports.

## **VI. Exceptions to Bank policy**

- 6.1 None

## **VII. Environmental and Social Strategy**

- 7.1 This TC will not finance feasibility or pre-feasibility studies of investment projects nor associated environmental and social studies; therefore, it does not have applicable requirements from the Bank's Environmental and Social Policy Framework (ESPF).

### **Required Annexes:**

[Request from the Client - CO-T1674](#)

[Results Matrix - CO-T1674](#)

[Terms of Reference - CO-T1674](#)

[Procurement Plan - CO-T1674](#)