CONVENING ON ALIGNING COLOMBIA'S FINANCIAL SYSTEM WITH SUSTAINABLE DEVELOPMENT
CEO Convening, 12 May 2015, 7 am – 8.30 am, Hilton Bogota
Technical Expert Convening, 12 May 2015, 8.30 am – 12.10pm, Hilton Bogota

Meetings Summary

The Colombian Ministry of Finance, the International Finance Corporation (IFC) and the United Nations Environment Programme's Inquiry into the Design of a Sustainable Financial System (UNEP Inquiry) convened two meetings with the Colombian financial sector in collaboration with the local consulting team (conTREEbute and Carlos Flórez) to present the findings of the study "Aligning Colombia's Financial System with Sustainable Development", and discuss the risks, opportunities, and potential solutions to further align the financial system with sustainable development challenges. These initial meetings were the first sector-wide discussions on sustainability and reaffirmed the leadership and innovation that is the hallmark of the financial sector.

The following is a summary of the key messages and next steps from the both the CEOs discussion and the technical workshop.

Key messages from both sessions:

- **Social and environmental variables must be included in the decision-making process:** It is important to realize that social and environmental issues can create risks and opportunities, and hence should be included in the financial sector's decision-making processes. Governance issues have grown in significance for investors in recent years as they can influence returns on their investments – the same approach is needed for environmental and social issues.
- **Private and public sector should work together to achieve a greener economy:** The faster a country starts including sustainability in the agenda of the financial sector, the easier developing a greener economy will be. An ideal scenario based on international experiences is one where the government creates an enabling environment for the private sector to embrace sustainable practices, and green investments do not rely exclusively on tax breaks.
- **Innovation in public policy is required:** Some basic policy signals and frameworks appear to be necessary for sustainable finance to advance in Colombia – disclosure policies, tax breaks, preferential interest rates, and other incentives should be carefully explored.
- **Public policy must be predictable:** Private players in the financial and real sector must be able to adapt their business progressively to fit social and environmental rules and regulations. The Ministry of Finance and the Ministry of Environment have an important role as catalyzers of this process through credible and predictable policies.
- **Education for the financial market is key**: Educating the financial sector is key to advance their understanding of social and environmental risks and how to integrate them into investment decisions.
- **Significant opportunities exist to incorporate sustainability**: The planned large-scale infrastructure projects in Colombia are a good opportunity to showcase how including environmental, social and governance (sustainability) criteria into project evaluation can result in better risk management and an integrated approach to assessing profitability.

- **There are signs of strong commitment and general optimism around sustainable finance:** There is broad commitment from different players across the financial industry around this agenda and they remain optimistic about the evolution of sustainable finance in Colombia.
- **Importance of increasing convenings and analysis:** Initiatives such as the IFC and UNEP Inquiry report on Colombia and multiple convenings are useful opportunities to broaden and deepen the debate around sustainability in the financial system and move the agenda forward, by bring together actors from across different types of institutions to share their perspectives and build awareness.

Regional experience of promoting sustainability:

- Mario Sergio, Head of Institutional Partnerships at FEBRABAN in Brazil, presented the Brazilian experience in green finance, including state-led regulatory initiatives and self-regulation measures that are being implemented. Conclusions from their research on the State of the National Financial System and the Green Economy (2013) and on capital allocations that incorporate social and environmental risk analysis, are aligned with the messages in the Colombian report:

  - Positive and negative environmental externalities need to be reflected in prices across the real economy.
  - There is a lack of uniformity and comparability of data; in particular there is low availability of data and understanding on the specific processes and products for the Green Economy.
  - The creation of a pipeline of good projects needs to happen alongside increasing the integration of ESG analysis in pension fund managers and insurance companies' investment decisions.
  - Necessary to review financial regulations for biases against environmental projects and/or for missed opportunities in green economy; legal uncertainties related to socio-environmental obligations need to be reduced.
  - Improving environmental risk management in bank lending is needed.
  - Although a consistent methodology to measure environmental and social impacts is not available, the Bovespa Index shows that companies incorporating ESG issues have had a better performance than those that are not.
  - National and international dialogues are needed on the effectiveness and experience of economic policy instruments such as taxation, fiscal incentives and regulation to increase sustainability and foster sustainable and innovative sectors.
  - A globally standardized methodology is needed to monitor resources allocated to the green economy along with a global discussion on capital allocation for socio-environmental risks.
  - Dialogues between the financial industry's professional associations need to be fostered on topics related to sustainable development.

- Paul Collazos, Head of Specialized Lending Risk Department, Superintendency of Banks, Insurers and Private Pension Fund Managers of Peru, presented their experience of integrating social and environmental risks in banking through financial regulation.

  - While Peru's GDP per capita has tripled in the last decade and mining has become an important engine of investment, the number of social conflicts has also tripled, resulting in delays and suspension of projects and consequently the probabilities of credit defaults in those projects have increased.
  - Since environmental and social risks will inevitably end up on some investor or lender's balance sheet, banks should direct attention towards this and the regulators must intervene, as this is an important source of systemic risk. Social conflicts should be tackled through environmental and social risk

management, which is a cost effective solution. Incentive-compatible requirements, disclosure and standard supervision techniques will ensure compliance.

- Regulation design might consider the borrower as the target, and not only the banks. Identification of social conflict risk factors, establishing baselines, likely impacts, preventative measures and grievance mechanisms, allows for risk categorization, and commitments to improve the quality of dialogue engagement with communities and management plans to reduce impacts and improve preventive measures.
- Peru's experience recommends better social and environmental risk management as this results in a leveled playing field so that lenders are not forced to compete offering lenient standards; improved corporate governance within banks; a lower rate of contagion of negative consequences derived from environmental and social risks; further impetus for voluntary initiatives and development of professional capabilities.

Colombian initiatives to promote sustainable finance:

- Javier Sabogal representing the National Department of Planning presented efforts to centralize access to international and national financial resources as well as tools and analysis. Monitoring, evaluation and analysis is underway on how public and private resources available for green initiatives are used. The Department is working through SISCLIMA to align private sector efforts with public initiatives. Work is also underway to prepare Colombia to access Green Climate Fund resources.
- Mauricio Mira, Green Business Director at the Ministry of Environment, presented a range of pragmatic solutions they are implementing including strengthening green entrepreneurship, partnering with the Chamber of Commerce, developing a platform to link green projects/businesses seeking resources with the available suppliers of credit. He highlighted the need to educate the private sector about advantages of being green, which can include better strategic position, lower costs and increased sales.
- Jessica Jacob, Director of Social and Environmental Responsibility at Findeter presented the evolution and scale-up of the Green Protocol. The initial phase has been focused on strong participation by banks, with future plans being focused on including other financial subsectors such as pension funds and insurance companies. She highlighted the importance of establishing concrete indicators to measure progress and communicating results.
- Doris Arevalo, Director of Business Intelligence Unit at Bancóldex presented the experience of implementing a social and environmental risk management system (SARAS for its acronym in Spanish). She indicated that environmental risks should be seen as just another risk that generates caution in banks, and that accurate measurement of green projects is difficult as many of them are not classified as such and are therefore financed as business-as-usual by banks. She identified that big projects such as electric public transportation require incentives to start and to reach the appropriate scale.
- Alejandro Navarro, Latin SIF and Sustainalytics Director in Colombia, commented that including ESG assessments in the investment review and decision-making processes is key, to assess the impact of such factors on returns. The LatinSIF in partnership with Bloomberg, the Colombian Stock Exchange and Global Reporting Initiative (GRI), is developing initiatives and tools to augment the ESG information available for investors and companies. They are simultaneously educating financial journalists and practitioners to generate and expand ESG knowledge and capabilities.

Feedback from the audience:

- The Government can act as a catalyst by advancing the use of green criteria in their procurement policy "Colombia Compra Eficiente".
- Despite advancements in Colombia, there remains scope for improvement in corporate disclosure practices, which remain limited when compared to financial institutions in e.g. the UK.
- Environmental regulation in Colombia is continuing to evolve and the banking sector needs new capabilities to act as a potential control point to verify borrowers' compliance with environmental and social standards. Banks also require stronger frameworks to understand and manage social and environmental risks.
- Investors are starting to demand that ESG factors be incorporated in the projects they invest in, but this is far from being a universal practice. Education about ESG factors should be a priority for investors.
- Such dialogues need to be replicated and scaled to reach wider audiences and share these messages. There is also a need to adapt these messages to small and medium enterprises (SME's), which account for around 92% of the economy.
- Small enterprises can have big impacts on the environment and banks generally have difficulties in lending resources to them. Therefore, it could be difficult to transfer environmental and social criteria to their activities.
- Civil society actors and NGOs are an important part of the economy but are not adequately reflected in the study. These actors can help ensure that resources obtained from investors and lenders are used properly.

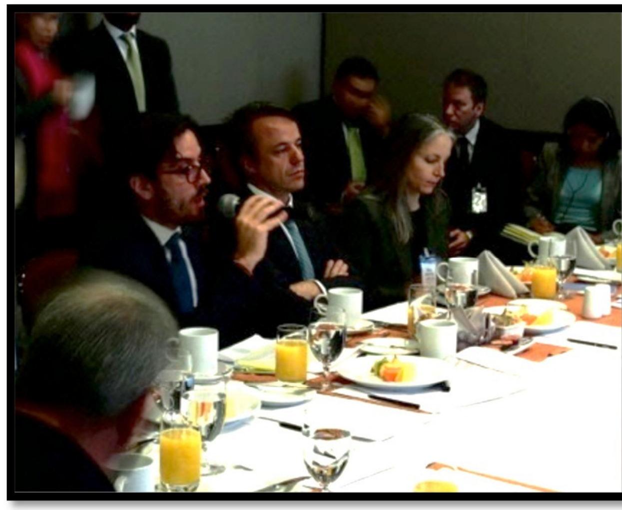
Conclusions and proposed next steps:

- Many of the necessary catalysts suggested in the report are already present in the Colombian economy and ready to be leveraged further. The costs arising from the impacts of "La Niña" showed the magnitude of environmental risks materializing and the need to manage these risks in future. Moreover, the 4G infrastructure projects are to be financed partially by international investors and they will likely influence the degree to which sustainability considerations are incorporated into these projects.
- Climate change should be approached from the perspective of both risk and opportunity. Regulation should work to maintain a healthy financial sector that avoids systemic shocks, but also allow for opportunities to be pursued. Ignoring ESG factors can lead to the materialization of risks in the medium and long term.
- There are different levels of progress within the financial sector on sustainability issues. The challenge is to bring the whole sector to a similar level of understanding, and enabling all actors to incorporate ESG factors into their business strategies.
- The approach should be holistic, targeting not only the financial institutions, but also the related regulations and institutions corresponding to the real economy (industry, agriculture, transportation, etc.).

Based on this, three areas of focus are foreseen in the short term:

1. **Leveling the playing field.** Financial sector associations such as Asofondos, Fasecolda and others should work closely with initiatives being championed by the banking sector (Asobancaria) and the Green Protocol.
2. **More communication and dialogue:** Emphasis should be placed on communicating better so that these topics reach other relevant stakeholders in the financial sector, real sector firms, and the general public.
3. **Clear framework:** Providing a clear framework around sustainable finance and the appropriate tools that can leverage the role and engagement of new players and stakeholders in the financial and real sectors.

High-Level Session
Seating down and from right to left:
Irene Arias, IFC Director of Latin American and the Caribbean Region; Pablo Vieira, Deputy Minister of Environment; Elliot Harris, UNEP Assistant to the Secretary General and Director of the New York Office.



High-Level Session
Seating in the front and from right to left:
Irene Arias, IFC Director of Latin American and the Caribbean Region, Andrés Escobar Arango, Deputy Minister of Finance; Pablo Vieira, Deputy Minister of Environment.

David Salamanca
Director at the Financial Regulation Unit (URF) - Ministry of Finance.

Experts Session
From right to left:
Javier Sabogal from the United Nations Development Program (UNDP); Doris Arevalo, Director of Business Intelligence Unit at Bancóldex; Jessica Jacob, Director of Social and Environmental Responsibility at Findeter; Mauricio Mira, Green Business Director at the Ministry of Environment; Alejandro Navarro, Latin SIF and Sustainalytics Director in Colombia.