

Environmental and Social Strategy

Savings and Credit Cooperative *Jardin Azuayo* “Credit for Community Development”

I. Transaction Overview

- 1.1 The proposed facility is a US\$ 5 million OMJ loan to the Savings and Credit Cooperative *Jardin Azuayo* to support the construction of social infrastructure for low-income rural communities in the south of Ecuador (the Project). The loan will contribute to the cooperatives’ line “Credits for Community Development”, which amounts to US\$10 million on total and channels funds to municipalities, parochial boards, civil society organizations and community associations (the final borrowers).
- 1.2 More specifically, through this line *Jardin Azuayo* will finance a variety of basic social infrastructure projects to serve local communities, such as: the rehabilitation and expansion of public schools, the improvement or construction of educational and sport facilities (for example chemistry, physics and IT laboratories), the construction or redevelopment of marketplaces, the improvement of irrigation systems and glasshouses, water treatment, the rehabilitation of community parks and other leisure areas, as well as the improvement of streets and small roads, among other possible social infrastructure works. The IDB proposed loan is for a 5 year tenor and is expected to finance nearly 250 new projects in different cantons of the selected provinces of Azuay, Loja, El Oro and Morona Santiago¹. The projects will be co-financed by the final borrowers, and will imply the participation of local communities in the approval, use and supervision of credits, including in the construction works themselves. The final borrowers will be ultimately responsible for the implementation of their respective projects. Interest rates will be determined based on actual market rates.
- 1.3 *Jardin Azuayo* is a regulated, registered not-for profit private entity established with the contribution of 120 financing members in 1993 to support reconstruction activities following the Josefina landslide. The cooperative manages and leverages local saving funds to channel them as financial services for the development of housing, social infrastructure works and microenterprise support. It has previously implemented a Technical Cooperation (TC) financed by FOMIN (ATN/ME-8078-EC, US\$431,000), which aimed to strengthen the cooperative’s institutional and financial capacity to serve new markets. The results of this TC’s evaluation were positive. *Jardin Azuayo* is among the seven cooperatives that have been selected by the Rural Finance Network as a “Model of Governance for Rural Development” to be used in a case study financed by the Ford Foundation.

¹ Cantons are the second-level administrative subdivisions of Ecuador, after the Provinces. The population of a canton in the Project area ranges from 3,000 to 40,000 inhabitants.

II. Environmental and Social Impacts and Risks

- 2.1 Given that proposed Project is a financial intermediation, it is classified under Directive B.13 (Noninvestment Lending and Flexible Lending Instruments) of the IDB's Environment and Safeguards Compliance Policy and is not subject to an environmental and social impact categorization. *Jardin Azuayo*, as the first tear borrower, will be responsible for the compliance with IDB's environmental and social safeguards and will have to comply with IDB's environmental and social requirements for all projects financed with IDB proceeds, which includes not financing any of the products or activities that are part of the IDB list of excluded activities for Structured Corporate Finance operations.
- 2.2 The Potential Environmental, Social, Health and Safety (ESHS) and labor risks of this operation are associated with the infrastructure works to be financed by *Jardin Azuayo* and co-financed by the final borrowers. Given the nature and context of the activities to be financed (i.e. infrastructure works within communities containing a relatively high proportion of low-income populations, which are in general more vulnerable to impacts and risks but who also benefit more from improved social services) the impacts could range from minor to medium in importance and scale.
- 2.3 *Positive direct and indirect impacts.* Several positive impacts are expected from the improvement, expansion or addition of local social infrastructure. For example, aside from less quantifiable impacts (for example the improvement of the community's well being and quality of life through an ameliorated environment), the project can ultimately contribute to higher school attendance rates and better results from students, and increase in local income from improved tourism and agricultural infrastructure, as well as a reduction of health problems through better sanitation.
- 2.4 *Negative direct and indirect impacts.* At the same time, there may be negative impacts on the environment as well as on the health and safety of local populations. These impacts could be direct (i.e. immediately associated with the construction works themselves) or indirect (i.e. when the new or remodeled infrastructure causes changes that affect populations in a negative way). There is a variety of possible negative direct impacts given the variety of infrastructure than can be financed through the project and of the population it will target within the community (i.e. the community as a whole but also children specifically). Some of the most likely impacts and risks are: an increase in air and water and noise pollution, accidents due to construction works, to unsafe construction and facilities, or to low safety standards; child labor, impacts on human health due to low sanitary standards (in market places for example), changes of urban land use not adequately consulted with the local population, violation of labor laws (for labors hired for construction works). These impacts and risks will be further analyzed during the due diligence and the team will explore and agree with the

borrower on ways to manage and mitigate such risks. The ESMR and a section of the loan agreement will reflect how these risks and impacts will be managed and mitigated by the borrower.

III. Strategy for Environmental and Social Due Diligence

3.2 As part of the due diligence process, the IDB will analyze the environmental and social aspects of this transaction to determine any potential environmental, social, health and safety, and labor requirements. The Bank will establish whether appropriate environmental and social procedures are in place at *Jardin Azuayo* to appropriately assess and manage these potential impacts and risks. The environmental and social due-diligence will focus on the components listed below and will attempt to identify areas where the Bank's participation could result in additionality by promoting better management and good practices related to environmental and social issues:

- i. An assessment of *Jardin Azuayo*'s involvement in activities that could represent a reputational risk to the IDB.
- ii. An identification of the key ESHS and labor legislation applicable in Ecuador.
- iii. An assessment of the compliance of *Jardin Azuayo*'s projects with all ESHS and labor legislation applicable in Ecuador, including the Fundamental Principles and Rights at Work and with any other international labor organization conventions and treaties which have been ratified by Ecuador.
- iv. A review of the main typical social and environmental issues and impacts found in the rural cantons of the selected project provinces, including labor related issues and compliance with applicable legislation.
- v. An assessment of typical municipalities' and other final borrowers' capacity and means to identify, manage, monitor and mitigate environmental and social impacts, in order to establish mechanisms for support and institutional strengthening when necessary for the project.
- vi. Related to the above, an assessment of the adequacy of participation mechanisms that have been used by the final borrowers in the project area, in order to build upon them and to improve them for successful project implementation.
- vii. An assessment of *Jardin Azuayo*'s credit evaluation, approval and monitoring procedures to manage environmental and social liabilities, impacts and risks of its loan operations. This assessment will also evidence the means (human and financial resources) that are in place to implement such procedures and

Jardin Azuayo's experience and capacity to implement environmental management tools.

- viii. An evaluation to ensure an appropriate inventory of present environmental and occupational safety liabilities in *Jardin Azuayo's* facilities and operations, and if so, assess the adequacy of the action plan to properly resolve them.

The Environmental and Social Management Report and a section of the Loan Proposal will report on the team's environmental and social due diligence activities and show how the environmental and social risks and impacts will be managed and mitigated.