

## PROJECT ABSTRACT

<b>Project number:</b>	ES-0163
<b>Project name:</b>	Banco de Comercio Mortgage-Backed Security
<b>Country:</b>	El Salvador
<b>Issuer:</b>	Banco de Comercio de El Salvador, S.A.
<b>MBS Issue Amount:</b>	US\$50 million
<b>IDB Guarantee</b>	Up to US\$20 million (40% of issue)
<b>Department:</b>	Private Sector Department
<b>Status:</b>	Eligible for Bank's financing
<b>Estimated approval date:</b>	June 2004

### Project Description

The Project consists of the issuance by Banco de Comercio of mortgage-backed securities (the "Bond Issue") denominated in United States dollars in the amount of approximately US\$50 million. The Bond Issue will be placed in the local capital markets in El Salvador and, depending on the results of the due diligence process, in other capital markets in Central America. Proceeds from the Bond Issue will contribute to the funding of Banco de Comercio's mortgage lending program. As such, placement of the Bond Issue is expected to: (i) provide funding on terms consistent with the long-term nature of mortgage lending; (ii) support the **future** development of secondary mortgage markets in El Salvador (and possibly other Central American countries); and (iii) make available new investment opportunities to institutional investors.

Banco de Comercio, a privately owned bank with over **2,470** shareholders is the fourth largest bank in the financial system in El Salvador, as measured by total assets.

Funding for the Project will be provided by the proceeds of the Bond Issue that will benefit from a partial credit guarantee ("PCG") of up to US\$20 million issued by the Inter-American Development Bank ("IDB" or the "Bank"). The amount of the guarantee to be provided by IDB will not exceed the lesser forty percent (40%) of the face value of the total amount of the MBS. The PCG will provide the necessary external credit enhancement to the Bond Issue in order to obtain the required credit rating.

### Project Benefits

The Project will support a key local mortgage lender in the preservation and lengthening of its funding liquidity, which will positively impact the availability of long-term mortgage lending in El Salvador. Furthermore, the transaction will contribute to the development of a secondary mortgage market, a key component in the availability of long-term house financing to the general population.

The Project will also contribute to develop capital market instruments. By supporting the issue of these types of securities as a source of long-term funding and a diversified investment opportunity for institutional investors, the transaction supports the development, deepening and diversification of

the capital markets.

## **IDB Participation**

The Project is consistent with the Bank's strategy for El Salvador that emphasizes supporting the development of the financial sector by using the various instruments at the Bank's disposal, particularly the Private Sector Department. As such, the use of the IDB's PCG is consistent with such strategy, as the Project is supporting the development of housing policy instruments to improve primary and secondary mortgage markets and the development of capital markets instruments.

The participation of the Bank is necessary to provide the external credit enhancement necessary to obtain the required credit rating of the Bond Issue to extend the average tenor of funding of Banco de Comercio that is consistent with the long-term nature of mortgage lending. Without the support of a multilateral institution, such long-term tenor for a regional security is unavailable.

## **Environmental and Social Strategy<sup>1</sup>**

Banco de Comercio does not have a formal Environmental Management System (EMS), however, they are in the process of developing an EMS for long term subordinated loan signed with the DEG last year. Additionally, preliminary information provided by Banco de Comercio indicates that: (i) in their regular mortgage appraisal major environmental and social aspects and potential liabilities are considered, and (ii) Banco de Comercio facilities are compliant with all relevant environmental and safety legal requirements and its Safety Department has developed a Contingency Manual for the Bank's facilities.

Based upon the nature of this Project, there should be limited direct environmental, social, or H&S impacts or risks, and thus no environmental assessment is required. The potential key environmental, social, health and safety, and labor issues and risks associated with the Project could include (i) Banco de Comercio's environmental credit risks and (ii) IDB Reputation Risks associated to Banco de Comercio or sub-borrowing Companies environmental, social, H&S, and/or labor practices.

Environmental Credit Risks refer to potential negative effects on Banco de Comercio's ability to repay the IDB because of: (i) risks due to Banco de Comercio's credit programs associated with the reduction in mortgage asset values or property guaranties/securities due to environmental or social issues (e.g. environmental liability); and (ii) risks associated with Banco de Comercio's facilities and operations, such as environmental liabilities in their buildings/offices due to PCB transformers, asbestos, lead paint, etc. or Banco de Comercio's employees having occupational health and safety

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<sup>1</sup>This Environmental and Social Strategy (ESS) is being made available to the public in accordance with the Bank's Policy on Disclosure of Information. The ESS has been prepared based primarily upon information provided by the project sponsors and does not represent either the Bank's approval of the project or verification of the ESS's completeness or accuracy. The Bank, as part of its due-diligence on the feasibility of the project, will assess the environmental and social aspects. This assessment will be presented in the project Environmental and Social Management Report, prepared by the Bank, and will be made available to public prior to consideration of the project by the Bank's Board of Executive Directors.

problems due to working conditions/environment (e.g. inadequate emergency preparedness, lack of fire exits, etc).

Reputation Risks are associated with Banco de Comercio's involvement with projects, companies or activities considered unacceptable to the IDB such as (i) long term financing in large project where environmental, social and H&S impacts have gone unmanaged; (ii) Banco de Comercio's finance application and analysis process that is not equitable, fair, and unbiased in terms of social factors (e.g. gender, age, sex, ethnicity, or cultural heritage etc.); and (iii) significantly deficient labor practices by Banco de Comercio or sub-borrowing Companies.

The Bank, as part of the due diligence process, will analyze the environmental and social aspects of the Project and establish environmental, social, health and safety, and labor requirements in the Partial Credit Guarantee Proposal for review and approval by the Bank's Committee on Environment and Social Impact (CESI). The environmental and social due-diligence will specifically include: (i) an assessment of Banco de Comercio's compliance status with the applicable country (national, state, municipal) environmental, social, H&S, and labor regulatory requirements; (ii) an assessment of the sufficiency of current credit appraisal, approval, and monitoring procedures to manage environmental and social liabilities, risks and/or impacts of loan/mortgage operation, or determine the need to include this activities in the Environmental Management System (EMS) currently being prepared; (iii) an evaluation to assure an appropriate inventory of present environmental and H&S liabilities in Banco de Comercio's facilities and operations, and if they exists, assess the adequacy of the action plan to properly resolve them; (iv) an evaluation to ensure that Banco de Comercio has adequate H&S and Contingency Plans and procedures (i.e. emergency response programs, building evacuation drills, etc) including their technical adequacy, adequate level of training, and sufficient resources to ensure adequate implementation; (v) an evaluation of the Banco de Comercio's compliance with the Fundamental Principles and Rights at Work and with any other international labor organization conventions and treaties which have been ratified by El Salvador, to determine presence of any existing major labor problems associated with Banco de Comercio, and whether they practices fair and unbiased labor practices related to sex, age, ethnicity, cultural heritage, and collective bargaining; Banco de Comercio must have (or develop) written procedures to assure adequate hiring procedures and treatment of employees; and (vi) an assessment of the adequacy of Banco de Comercio's procedures to ensure that loan/mortgage and/or foreclosure procedures, finance application and analysis process is equitable, fair, and unbiased in terms of social factors (e.g. age, gender, cultural heritage, etc).

Current procedure should at a minimum (i) be able to determine borrower's eligibility according the IDB's excluded activities, (ii) include in the loan/mortgage application and analysis process (i.e., underwriting guidelines and risk review process) consideration of environmental or social aspects, and assess potential environmental financial/credit risks and liabilities that may be associated with the properties, (iii) determine borrower's compliance with the applicable environmental, H&S, and labor regulatory requirements, (iv) apply loan/mortgage insurance to cover environmental issues (e.g., soil and ground water contamination, lead based paint, asbestos, polychlorinated biphenyl compounds) and natural hazards (e.g., fire, tornadoes, hurricanes, floods, seismic events), and (v)

count with mortgage credit officers qualified and trained to identify potential environmental, social, H&S, and labor issues/liabilities.