## Eco. Business Annual Review – 2020 Performance

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| **Title:** Eco. Business Fund (EBF) | | |
| **Programme Value £ (full life):** £32.6 million | | **Review date:** 2021 |
| **Programme Code:** GB-GOV-GB-7-P00052-ICF-P0003-ECO.B | **AMP (Aid Management Platform) start date:**  Fund inception: January 2015  Promissory Note (£20m): December 2015  Further investment (£12.6m): December 2019 | **AMP end date:**  Provision for the Department for Environment, Food and Rural Affairs (Defra) investment to be returned in December 2030 and 2035 respectively |

**Summary of Programme Performance**

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| Year | **2017** | **2018** | **2019** | **2020** |
| Overall Output Score | **A** | **A** | **A+** | **A** |
| Risk Rating | **Moderate** | **Moderate** | **Moderate** | **Moderate** |

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| DevTracker Link to Business Case: |  |
| DevTracker Link to results framework: |  |

**A. SUMMARY AND OVERVIEW**

**Description of programme**

The eco.business Fund (EBF) was set up in December 2014 by KfW, the German Development Bank, Conservation International and Finance in Motion (FiM – the Fund Advisor). The EBF´s mission is to promote business and consumption practices that contribute to biodiversity conservation, to the sustainable use of natural resources, mitigation of climate change and adaptation to climate change impacts. The Fund has two sub-funds, one for Latin America and Caribbean (LAC) and the other for Sub-Saharan Africa (SSA), which was launched mid-2019. Defra’s investment is in the LAC sub-fund. FiM acts as an advisor to the Board of Directors – the independent panel nominated by the Fund’s shareholders. The Board has the ultimate decision-making authority, provides scrutiny for investments, and decides on projects and strategic matters for the Fund.

This is the fourth Annual Review (AR) of EBF. The performance of the programme has been assessed both qualitatively and quantitively against the logical framework, which contains annual targets. In addition to ARs, performance reviews are undertaken by FiM, the programme delivery partner. These are reported quarterly to an independent Board of Directors, where Defra sits as an observer. A financial report of the EBF is independently audited annually.

**Summary supporting narrative for the overall score in this review**

Summary of progress since January 2020

The LAC sub fund expanded further into the Andean region and Central America, with the first investment in Guatemala, and large investments in Honduras, El Salvador, and Costa Rica. The fund now operates across 8 countries (7 as of 2019) and 22 Partner Institutions (PIs) (19 as of 2019). The Sub-Fund closed its first direct investment in 2020, supporting sustainable shrimp production in Ecuador. Through the work of the Fund and the Development Facility (described below), at the end of 2020, 8.8 million tons of CO2 (absolute) were stored through agroforestry activities, 4.5 million m3 of water were saved, 430,000 hectares of farmland were under sustainable management, and 37,000 litres of herbicide use was avoided. To note for CO2 the fund measures both absolute and net CO2 storage. The above figure refers to absolute storage.

The outstanding portfolio (principal value) had increased from US Dollar (USD) 331.1m at the end of 2019 to USD 394.9m at the end of 2020. On top of the USD 394.9m, the balance of outstanding exposures offloaded (sold) to Calvert Impact Capital totalled USD 37.9m at year end 2020 (see output 4 for detail). Hence, there was growth in the portfolio in 2020 of USD +62m (and USD +99.8m if there had been no exposures offloaded to Calvert). The total cumulative disbursements since fund inception up to the end of 2020 was USD 584.4 million.

The EBF has USD $494.4m in committed funding and since inception has disbursed 21,447 sub loans (USD $1,862m). The fund is now a recognised financier and knowledgeable partner in a range of sustainably focussed activities in a large and sectorally diverse region.

The Development Facility

The Development Facility (DF) is a separate entity that sits alongside the EBF’s investment portfolio. The DF provides grant finance directed at Technical Assistance (TA) projects. Typical examples of these projects include promoting environmentally sustainable land-use practices within small businesses to enable environmental sustainability standards to be achieved, sponsoring events, running capacity building workshops, embedding lending practices and/or implementing Environmental and Social Management Systems (ESMS). In 2020 the DF spent USD 3.9m on 73 individual projects. This is described further in output 3.

The above demonstrates that investment into the EBF continues to positively contribute to Defra’s and Her Majesty’s Government (HMG) strategic climate objectives.

**Major lessons and recommendations for the year ahead**

1. The Fund should engage with Defra over the next year to aid understanding of why output indicator 1.2 was marginally not met, provide an indication of future commodity development and discuss steps to ensure the 2021 target is achieved.
2. Considering current Defra logframe targets are set to 2022, it is recommended that Defra work with the fund to produce future targets/projections in the logframe to assess the expected progress of the fund. For outcome indicators 1.5 and 1.6 which correspond with ICF KPIs (Key Performance Indictors) 11 and 12 we recommend recalculating the targets in line with the updated 2019 methodology for the calculation of Defra attribution to these results. This will ensure consistency and allow Defra to track its contribution to the fund more accurately. It may also be advisable for the Fund to work with Defra to revise Defra’s logframe targets upwards for output indicators 2.1 and 2.2 to account for the fact that the 2022 targets have already been exceeded and to continue to build on the success of the fund in this area.
3. The Fund should continue to develop the pipeline and secure approval from the Development Facility Committee for TA projects for 2021 in order to achieve the target for 3.1 and continue to provide high quality, consistent TA across projects and to PIs.
4. Defra should undertake further work to consider best practice for impact investment funds in measuring biodiversity impacts, working with the fund managers and other industry practitioners.
5. Defra should undertake an external evaluation of the programme’s performance since initial investment, as referenced in the Annex 3 of the Subscription Agreement. The external evaluation should consider how the fund is progressing towards its outcomes and final impact through its activities and outputs.
6. A key priority for Defra International Climate Finance/ODA funding going forwards is supporting gender equality and empowerment. It is noted that EBF plan to develop a gender strategy for the fund to expand the work it has achieved to date and encompass additional strategies to address climate change by supporting female empowerment from a financial perspective. It is recommended that Defra work with EBF to help develop the gender strategy that is being developed.

## B: THEORY OF CHANGE AND PROGRESS TOWARDS OUTCOMES

EBF manages its impact based on a Theory of Change (ToC) and in alignment with the [Operating Principles for Impact Management](https://www.impactprinciples.org/). The ToC considers four levels – activities, outputs, outcomes, and final impact. Some elements of the ToC are directly controlled by the Fund, for example raising public and private capital or providing technical assistance to financial institutions (activities and outputs). However, some are a result of both the fund and external factors, for example an increased integration of sustainability considerations in investment and production practices in the short term and scaling sustainable investment and production practices in the long term (e.g., outcomes and final impacts).

Given the nature of the fund (lending to financial institutions who then on-lend to end borrowers) and the complex environments in which the fund’s investees and stakeholders operate in, the EBF does not attribute the total change happening at outcome and final impact level exclusively to the Fund’s contributions. Instead, the ToC focuses on the processes that are likely to be triggered by the Fund’s activities and how these lead to the final environmental and socio-economic impacts. This causal analysis draws on evidence from financial institutions, industry networks, international institutions, academia, and conservation organisations. A detailed description of the ToC can be found [here.](https://www.ecobusiness.fund/fileadmin/user_upload/impact/Theory_of_Change/EBF_Theory_of_change_2019.pdf)

The Fund’s [Impact Framework](https://www.ecobusiness.fund/fileadmin/user_upload/impact/the_pathway_to_impact/ecobusiness_Fund_Impact_Framework_Growing_Impact_2019.pdf)  complements the ToC and illustrates how the Fund meets its objectives by connecting actions to defined outcomes and final impacts. It also maps out how progress is measured and reported.

**Annual outcome assessment**

In Defra’s logical framework for the EBF, outcome indicators are defined as:

1. EBF's success in contributing to biodiversity conservation, the sustainable use of natural resources and climate change adaptation and mitigation; and this success creating an incentive for others to also act towards these goals.
2. Level of behavioural change embedded in downstream lenders and Financial Institutions (FIs).

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| Outcome | Outcome indicator (all results cumulative) | Milestone 2020 (Defra review) | Achieved 2020 (fund level) |
| 1. EBF's success in contributing to biodiversity conservation, the sustainable use of natural resources and climate change adaptation and mitigation; and this success creating an incentive for others to also act towards these goals. | 1.1 Amount of water savings entirely or partly attributable to the intervention of the EBF (millions of cubic metres) | 7.5 | 4.5 |
| 1.2 Level of funding provided by FIs to businesses that adopt sustainable practices (M $USD) | 1000 | 1862 |
| 1.3 Land sustainably managed through the EBF's portfolio (Ha) | 250, 000 | 430, 000 |
| 1.4 Land held by sub-borrowers committed to deforestation-free activities in EBF portfolio (Ha) | 200, 000 | 260, 000 |
| 1.5 ICF KPI 12: Volume of private finance mobilised for climate change purposes as a result of ICF funding (M $USD) | n/a | n/a |
| 1.6 ICF KPI 11: Volume of public finance mobilised for climate change purposes as a result of ICF funding (M $USD) | n/a | n/a |
| 1.7 Number of jobs supported by sub-borrowers as a result of EBF support† | 400, 000 | 452, 000 |
| 1.8 ICF KPI 6: Net CO2 sequestration as a result of EBF support to agroforestry (t) | 1, 000, 000 | 1, 000, 000 |
| 2. Level of behavioural change embedded in downstream lenders and FIs. | 2.1 Number of sub-borrowers supported by EBFs PIs to incorporate sustainable practices | n/a | n/a |
| 2.2 Number of FIs that have changed their policies to incorporate sustainability as a qualifier for lending | Qualitative assessment |  |
| 2.3 The level of sub-borrower staff knowledge of the sustainable policies of their companies | Qualitative assessment |  |
| 2.4 The level of FI staff knowledge of the sustainable lending policies of their institutions | Qualitative assessment |  |

Progress on Outcome targets:

Through the work of the Fund and the DF by the end of 2020 1 million tons of net CO2 were stored through agroforestry activities (8.8m tonnes absolute), 4.5 million m3 of water were saved, 430,000 hectares of farmland were under sustainable management (a significant increase on 2019 due to the increase in new FIs starting to report), and 37,000 litres of herbicide use was avoided. For outcome 1.1 it is important to note that water savings are occurred when financing specific measures. Since the financing follows market demand, exact results are challenging to forecast.

The Fund is surpassing Defra targets in terms of the level of funding provided by FIs to businesses that adopt sustainable practices, land sustainably managed through the EBF's portfolio, land held by sub-borrowers committed to deforestation-free activities, leveraging private and public finance, jobs supported by sub-borrowers as a result of EBF support and sub-borrowers supported by EBFs PIs to incorporate sustainable practices. The target for CO2 emissions avoided was met exactly in 2020, while the target for water savings attributable to the intervention of the EBF was not met.

**Outcome 1 – Performance:**

Metrics within outcome 1 show that disbursements to FIs have exceeded the Defra target. Additionally, 260,000 (against a target of 200,000) of the total hectares under management are managed under agroforestry, forestry and silvopastoral systems, thereby supporting maintaining forest cover and contributing to EBF’s commitment to zero deforestation.

Three ICF KPIs have been selected for use at the outcome level, KPIs 6, 11 and 12 (Outcomes 1.5, 1.6 and 1.8). Outcomes 1.5, 1.6 and 2.1 are reported on by the Fund to Defra, but are not published due to their commercially sensitive nature. All three exceeded the targets set for them for 2021, 2x for KPI 12 and nearly 3x for KPI 11.

Additionality is taken into account by Defra for all interventions funded through ICF. This is to ensure there is a net change in impacts resulting from UK funding, other than the business-as-usual changes that would occur without UK funding. Ideally for most scenarios, the outputs would be compared to a suitable baseline or counterfactual scenario, so as to isolate the impact/additionality of a programme. For most programmes a conservative additionality rate of 50% is applied to the impacts.

For KPI 6, EBF calculate this KPI as the difference between absolute CO2 sequestration and CO2 sequestration for a baseline scenario. The baseline scenario estimates CO2 sequestration assuming the fund’s investments would not specifically target agroforestry systems but would reflect instead the share of production area of shade and non-shade systems prevailing at country level. This baseline figure changed slightly over time with countries naturally increasing their “under-shade” production of coffee and cocoa.

**Outcome 2 – Performance:**

Metrics within Outcome 2 show that the number of sub-borrowers is increasing.

As part of the work of the DF, over 604 bank officers were trained through various projects that assisted 19 PIs from 14 countries to increase financing of sustainable businesses. A total of 394,000 individuals were reached through events and other training activities co-sponsored or fully sponsored by the DF designed to promote sustainability in the region.

***Output level Summary***

Outputs have been decided based on the objectives of the EBF to promote business and consumption practices that contribute to biodiversity conservation, to the sustainable use of natural resources, and to mitigate climate change and adapt to its impacts. Outputs have been weighted in accordance with their importance to the success of the EBF and alignment with Defra ICF’s strategic priorities. The outputs below include the following progress highlights:

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| **Output no. and description** | **Performance summary** | **Score** | **Weight %** |
| **OUTPUT 1:** EBF has a diversified portfolio supporting a range of geographies and sectors. | * There was an expansion of the EBF portfolio into Guatemala, through a USD 20 million investment in Banco Agromercantil. * EBF has increased the number of FIs in its portfolio from 19 to 22 and realised its first direct investment. It further engaged private sector capital by selling USD 41 million of loans directly from its loan book. Through this innovative transaction, Calvert Impact Capital is directly supporting financing aligned with the Fund’s mission in the region. The freed-up capital is deployed for further disbursements in the region. | A | 35% |
| **OUTPUT 2:** Broad support to sustainability practices reflected in the composition of the portfolio. | * The number of sustainability standards used have increased over the year from 15 to 22, and the number of green list measures has risen from 20 to 32. * EBFs Partner Institutions disbursed over 7100 sub-loans, amounting to a total of USD 676.7 million in 2020. | A+ | 35% |
| **OUTPUT 3:** Provision of continuous and sufficient TA. | * At the end of 2020, the EBF DF had 16 ongoing or outstanding projects, supporting 15 existing and 2 new Partner Institutions (PIs). * From fund inception to the end of 2020 the DF has completed 56 individual TA projects, with a total spend of USD 4.11m on TA. | A | 15% |
| **OUTPUT 4:** Improved partnerships and development of activities with other sector stakeholders. | * Over the course of 2020, USD 126 million in additional funding was secured, translating into a total of USD 494.4 million funding available at year end. * The Fund made its first ever corporate transaction, providing a loan of USD 15 million directly to Industrial Pesquera Santa Priscila, the largest shrimp producer in Ecuador. | A | 15% |

**Describe where the programme is on/off track to contribute to the expected outcomes and impact. What action is planned in the year ahead?**

The programme is on track to contribute to Defra’s expected outcomes and impact. In fact, in many areas targets are being surpassed. It is recommended that Defra work with EBF to revise the targets in the Defra logframe for the next few years upwards in line with the current trend in results. Additionally, this will raise ambition of the fund and hopefully lead to greater results at final impact level, evidencing the validity of the theory of change. It must be noted, though, that some indicators are difficult to accurately set targets for and are dictated by market conditions and further investment. Defra will work with the Fund to ensure realistic targets are set based upon the best available evidence.

The Fund’s strategic pillars are to: consolidate success, diversify growth, deliver on impact and become an agent of change. For 2021 the focus will be on further portfolio growth (including more direct investments), consolidation in existing markets and expansion to new markets, and increasing exposure and knowledge of key Fund sectors. There is a strong investment pipeline for 2021, and there are two tranches (USD 18m total) in Senior Notes by ASN Bank maturing in June and December 2021, expected to be rolled over jointly and topped up in Q3 2021. Further subscriptions by private investors in Senior and Subordinated notes are expected in Half 2 (H2) 2021. Currently the EBF Development Facility funds technical assistance work in Mexico but the main Fund has not made investments in Mexico; it is due to in 2021. There will be some changes to the EBF issue document proposed in H2 2021 and the fund will continue aligning with the EU sustainable finance agenda in terms of continued SFDR (Sustainable Finance Disclosure Regulation) compliance and EU taxonomy monitoring.

Despite the impact of covid-19 there are no changes in impact or the timetable of delivery for the programme.

**Justify whether the programme should continue, based on its own merits and in the context of the wider portfolio**

Based on the above analysis of outcome and output achievement, ToC and VfM analysis, the programme is performing well, continues to represent good VfM and fits with Defra’s ICF/ODA priorities including mobilising finance for nature and testing and demonstrating innovative investment models i.e. blended finance and technical assistance for implementation of sustainable agriculture. It is also working to address barriers to progress in climate change adaptation and sustainable livelihoods and transformational change of the financial system. It is therefore recommended that the programme continue.

## C. DETAILED OUTPUT SCORING

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| **Output Title** | EBF has a diversified portfolio supporting a range of geographies and sectors | | | |
| Output number: | | 1 | Output Score: | A |
| Impact weighting (%): | | 35 | Weighting revised since last AR? | No |

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| **Indicator(s)** | **Milestone(s) for this review** | **Progress** |
| 1.1 Number of financial institutions in the EBF´s portfolio | 17 | 22 |
| 1.2 Number of commodities supported | 21 | 20 |
| 1.3 Number of countries in which the Fund operates | 7 | 8 |

**Key Points**

There was progress against all the indicators except 1.2 since 2019, with targets exceeded for 1.1 and 1.3. Targets are on track to be met or have already been exceeded up to 2022.

Progress:

* The number of FIs in the EBF’s portfolio grew during 2020 from 17 to 22, with the Fund completing ten new investments amounting to a total of USD 167.5 million in commitments, of which USD 150 million was disbursed immediately in 2020.
* The Fund currently channels dedicated financing to local producers via selected local FIs, and in limited cases will provide direct financing for innovative, high-impact businesses and projects. One such example of the latter is the Fund’s first corporate transaction investment, which was a USD 15 million loan to Industrial Pesquera Santa Priscila, the largest shrimp producer in Ecuador. The loan will be used to implement measures that further reduce the company’s environmental footprint and resource use, as well as support sustainable production in the aquaculture industry, one of EBF’s four target sectors (the others being agriculture, forestry, and sustainable tourism). The bracketed figure in the table for 1.1 is the total plus the investment in Industrial Pesquera Santa Priscila.
* The commodity most supported in the Fund’s outstanding sub-loan portfolio at the end of 2020 was coffee , which demonstrates the success of the EBF in supporting the sustainability of this key Latin American crop. The “blue sector” (farmed fish and shrimp) represents the second largest commodity in the Fund’s sub-loan portfolio. This has been a recent focus area of the fund in recognition of the economic importance of this commodity in LAC (see also reference to first corporate transaction above).
* The Fund also entered a new country - Guatemala. It therefore now operates across among 22 Partner Institutions in 8 countries (Colombia, Costa Rica, Ecuador, El Salvador, Nicaragua, Panama, Honduras, and Guatemala). It is worth noting that as of 2019 TA has been provided in Mexico, but as there were no investments in Mexico as of year-end 2020 this is not reported as a country in which the Fund operates.

As of year-end 2020, the number of crops reported by Fund’s PIs was 20.

**Recommendation:** The Fund should engage with Defra over the next year to aid understanding of why output indicator 1.2 was marginally not met, provide an indication of future commodity development and discuss steps to ensure the 2021 target is achieved. It is noted that some PIs report crops supported under “various” which includes more than one commodity

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| **Output Title** | Broad support to sustainability practices reflected in the composition of the portfolio | | | |
| Output number: | | 2 | Output Score: | A+ |
| Impact weighting (%): | | 35 | Weighting revised since last AR? | No |

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| **Indicator(s)** | **Milestone(s) for this review** | **Progress** |
| 2.1 Number of sustainability standards represented in the portfolio of sub-borrowers | 15 | 22 |
| 2.2 Number of Green List measures represented in the portfolio of sub-borrowers | 13 | 32 |
| 2.3 Outstanding Amount (USD millions) invested in certified sub-borrowers\* | n/a | n/a |
| 2.4 Outstanding Amount (USD millions) invested in green list measures\* | n/a | n/a |

**Key Points**

There was strong progress against targets for both indicators 2.1 and 2.2 since 2019. Targets have already been exceeded for 2021 and 2022.

* To note, the bracketed figures in outputs 2.3 and 2.4 refer to the EBF share only, and the other figure includes the off-loaded amount of the existing portfolio to Calvert Investment Capital.
* The Fund’s [eligibility criteria](https://www.ecobusiness.fund/en/impact) for the use of funds include a combination of sustainability standards and activities under the green list (GL) (screened and pre-approved practices with a positive impact on sustainability) approach. The end-borrowers financed during 2020 by the EBF are mainly engaged in the production or transformation of coffee, sugarcane, and farmed shrimp. During 2020 the EBF further developed eligibility criteria for the sustainable tourism sector.
* Eligible labels financed throughout 2020 included Rainforest Alliance and the Fairtrade Standard for Small Producer Organisations.
* New Green List (GL) measures added to the portfolio in 2020 included: i) Recycling of agricultural waste that is otherwise disposed of (#31), ii) Dry sugarcane cleaning system (#10), iii) Biogas equipment (#34). When financing a new PI using the GL approach, EBF discusses and agrees with the PI which GL measures are the most appropriate. The actual financing then follows the fund’s market logic, based on the needs and interest of the end-clients.
* Amongst supported GL activities, the Fund’s PIs primarily on-lend for activities related to sustainable land use, production, and extraction practices.
* In 2020, the Fund’s PIs disbursed more than 7100 sub-loans, amounting to a total of USD 676.7 million being passed on to end borrowers (up from USD 385.9 million in 2019).
* At the end of 2020, the outstanding sub-loan portfolio stood at just above USD 429.2 million (up from ~ USD 300 million in 2019). This portfolio is allocated with ~80% to end borrowers that hold an eligible sustainability certification, and ~20% with eligible green list activities.

**Recommendation:** The Fund work with Defra to revise Defra’s logframe targets upwards for output indicators 2.1 and 2.2. to account for the fact that the 2022 targets have already been exceeded and to continue to build on the success of the fund in this area.

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| **Output Title** | Provision of continuous and sufficient Technical Assistance | | | |
| Output number: | | 3 | Output Score: | A |
| Impact weighting (%): | | 15 | Weighting revised since last AR? | No |

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| **Indicator(s)** | **Milestone(s) for this review** | **Progress** |
| 3.1 Number of on-going/outstanding TA projects | 27 | 16 |
| 3.2 Number of financial institutions supported | 15 | 19 |
| 3.3 Number of completed TA projects | 47 | 56 |
| 3.4 Budget spent on TA projects (USD million) | 4 | 4.11 (closed: 2.95, on-going 1.15) |

**Key Points**

There was progress against all the indicators except 3.1 since 2019, with targets comfortably exceeded for 3.2 and 3.4 and exceeded by a large margin for 3.3. for 1.1 and 1.3. Targets are on track to be met or have already been exceeded up to 2022. It is important to note that the underachievement of indicator 3.1 is a direct result of the overachievement of 3.3 (a target of 47 and progress of 56, an increase of 24 projects from 2019).

* The DF has carried out projects ranging from supporting PIs in strengthening their capacity to finance sustainable businesses, to activities that promote the implementation of sustainable practices and increase the fund’s visibility and influence in the region. At the end of 2020, the DF had 16 projects under management.
* The Development Facility (DF) provides added value to the main function of the fund – ensuring that FIs and borrowers are supported in gaining the tools and skills needed to implement and embed more sustainable agricultural practices. It aims to increase the impact of the fund through a variety of TA projects for promoting sustainable practices across three areas: impact and sustainability; enhanced eligibility; and knowledge sharing. For example, in July 2020 the DF published the first part of the “Practical Manual for the Implementation of Environmental and Social Management Systems (ESMS) in financial institutions,” which is publicly available. This is alongside the DF working with eight partner institutions in Ecuador, Panama, Costa Rica, and El Salvador in the development, update and/or implementation of their ESMS
* The results show that the underachievement of indicator 3.1 is due to the high completion rate of TA projects in 2020 (as evidenced in 3.3). The Fund is confident that the 3.1 target for 2021 will be reached as a number of new projects will be submitted to the DFC board for approval throughout 2021. One such example of an ongoing project in 2020 is the new project with Bancolombia to develop a new financial product that provides financing for sustainable cattle operations in Colombia. It aims to promote the implementation of sustainable practices within the cattle sector and will facilitate access to financing for cattle farmers committed to the conservation of forests, climate change mitigation and adaptation.
* At the FI level, the DF trained representatives from Banco Hipotecario in El Salvador to develop an impact framework by providing tools such as policy documents and procedures to measure the environmental and social impact of their investments. Additionally, the DF assisted Banco Hipotecario in the development of the app “AGRO,” designed specifically for small and medium clients in the agricultural sector. The app provides information that facilitates informed decision-making for producers, thus improving performance and decreasing environmental impact. The app also helps loan officers determine if a potential client in the agricultural sector is eligible for financing by measuring their overall environmental impact.
* Cumulatively, the Fund’s DF had 73 projects approved for a total budget of USD 3.9 million. This represents an increase of 0.9 million compared to 2019.
* In a uniquely challenging year, the DF also recorded the highest project execution since inception at USD 1.9 million.
* Key activities carried out in 2020 include:
  + Development and implementation of Environmental and Social Management Systems (ESMS) for 12 partner institutions (PIs) in Ecuador, El Salvador, Nicaragua, Honduras, and Panama. Of these, 5 PIs did not have an ESMS in place prior to working with the DF, 3 PIs did not have an E&S (environmental & social) team in place prior to working with the DF, 3 PIs automatized their ESMS and integrated it into the bank’s digital software, and 2 PIs incorporated IFC Performance Standards into their ESMS. The DF is facilitating and contributing to a sector-wide shift towards a green financial system that promotes environmental and social sustainability.
  + Piloting the Aquaculture Green List with two shrimp companies in Ecuador. This project includes: i) a diagnosis to identify gaps both companies need to fill to qualify for ASC certification as well as the Green List measures that could be implemented in both companies, ii) the creation of an action plan for the improvements that need to be implemented, and iii) the installation of more sustainable technologies to measure the environmental impact of incorporating these technologies into the production system. The DF completed the diagnosis to evaluate both companies’ current environmental performance, developed the action plan to guide activities to be implemented, and completed the Biodiversity Environmental Impact Assessment and a Participatory Social Impact Assessment.
  + Developed and launched a COVID-19 response package project for 8 PIs in Honduras, Nicaragua, Panama, Costa Rica, and Ecuador. This project aimed to assist PIs in addressing multiple challenges resulting from the COVID-19 crisis through a diverse set of technical support measures that bolster their ability to maintain operations, thereby continuing to finance business and consumption practices that contribute to biodiversity conservation, the sustainable use of natural resources, and mitigating and adapting to climate change.
  + Completed a study regarding the development of green financial products (GFPs). The purpose of this project was to develop a methodology to guide the design of GFPs for FIs in the region. The project also included a study pinpointing the areas of opportunity, thus creating a guiding map for the Fund’s work in this area.
  + Promoted the expansion of Nicaragua’s sustainable coffee frontier through a project with Asocafens, a coffee producer association whose members include clients from the fund’s PI Banco Lafise. The project aims to strengthen the association to manage its Destination of Origin and meet EU requirements to register their DO before the EU. The DF has worked in the development of the first half of documents, policies, and procedures set within the scope of the project.

**Recommendation:** The Fund should continue to develop the pipeline and secure approval from the Development Facility Committee for TA projects for 2021 in order to achieve the target for 3.1 and continue to provide high quality, consistent TA across projects and to PIs.

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| **Output Title** | Improved partnerships and development of activities with other sector stakeholders | | | |
| Output number: | | 4 | Output Score: | A |
| Impact weighting (%): | | 15 | Weighting revised since last AR? | No |

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| **Indicator(s)** | **Milestone(s) for this review** | **Progress** |
| 4.1 Number of external events organised by the EBF | 3 | 3 |
| 4.2 Number of events EBF has supported | 35 | 47 |
| *4.3 Number of investments realized by the Fund in partnership with other institutions (e.g., syndicated loans)* | *n/a* | *8* |
| *4.4 Investments realized by the Fund in partnership with other institutions (USD millions)* | *n/a* | *n/a* |

**Key Points**

The target for output indicator 4.1 was met and 4.2 was exceeded by a significant margin. was progress against all the indicators except

* In 2020 the EBF DF partnered with UNEP FI to co-host two webinar series, the first introducing the “Principles of Responsible Banking” framework and the second on “Climate Change: Risks and Opportunities for the Finance Sector.”
* In 2020, EBF launched the ‘Sustainability Academy’ with the objective of creating a knowledge sharing platform for financial institutions, producers, and the public tailored to the region’s specific context. The Sustainability Academy partnered with relevant actors in the region such as the Tropical Agricultural Research and Higher Education Center (CATIE, in Spanish), with which the academy hosted five seminars for the fund’s target audience and the public. The Sustainability Academy has also developed courses and hosted trainings for six PIs. The Sustainability Academy will continue creating new resources and offering different learning opportunities that will help both the fund’s PIs and their clients in promoting and adopting sustainable practices.
* It is worth noting that indicators 4.3 and 4.4 are not considered as part of the output scoring as they are not specific objectives of the EBF. However, they are still being measured as a matter of data collection. For output 4.4 the unbracketed figure is the EBF’s share of financing in syndicated loans and the bracketed figure covers the EBF’s total investments to PIs. In previous AR’s only the EBF’s share of financing was included. The EBF applies a market logic and will only enter a syndicated deal if all parameters match the fund’s rigorous requirements, therefore it is likely that the targets (based on assumptions about the market) were initially set too high. Even though they are not considered as part of the output scoring it may be worth revising the targets in line with the reality of market conditions.
* The Fund successfully managed the investment from a large commercial German Bank in 2020, which invested both in Senior Notes and Subordinated Notes, highlighting the Fund’s attractiveness to private sector investors, even during covid-19.
* Private investors have contributed a total of USD 157 million since the inception of the Fund, and at the end of 2020, private sector funding accounted for 32% of total funding.
* Over the course of 2020, USD 138 million in additional funding was secured, translating into a total of USD 494.4 million funding available at year end. The Fund clearly continues to mobilise additional funding, hence leveraging Defra’s first-loss capital.
* The Fund deepened its relationship with its existing investor Calvert Impact Capital (CIC) in 2020 by off-loading USD 42m of existing portfolio via a funded sub-participation by CIC in 5 outstanding loans at 50% each i.e. EBF continues to hold 50% of these loans (and the associated risks), while the rest transferred to Calvert. This is the first time a private investor is taking direct risk exposure to EBF LAC’s portfolio without first loss buffer. The use of loan participations is an innovative alternative to attracting new investors i.e., in addition to investing into the fund’s diverse portfolio, investors can acquire direct exposures from that portfolio. This transaction shows how to combine impact investing with mainstream financial instruments like loan participations. It places trust in the EBF’s underwriting standards and could create a signalling effect for other investors in the market. This is a clear example of how a private investor like CIC can leverage its partnership with EBF and contributing to mainstreaming conservation finance.
* The Fund made its first ever corporate transaction, providing a loan of USD 15 million to Industrial Pesquera Santa Priscila, the largest shrimp producer in Ecuador, which will be used to implement measures that further reduce the company’s environmental footprint and resource use, as well as support sustainable production.

**Value for Money ([VfM](https://dfid.sharepoint.com/sites/inSight-rules-smart/Documents/Smart%20Guide_approach%20to%20value%20for%20money.docx)) Assessment**

**Economy:**

As of 2020 Q4, the fund’s total expense ratio continued to decrease as percentage of average portfolio. The remaining income, once costs of the fund are covered, will be distributed to the shareholders with the more senior debt and shareholdings paid first before complementary shares are paid to junior shareholders due to the income waterfall. Dividend allocation totals to $686,890. Any dividends received by Defra are re-invested into the Fund.

**Efficiency:**

With a cumulative current fund level of 1,000,000 tonnes of carbon sequestered, EBF exceeded its target of 560,000 tonnes by 78.6% (as specified in the Business Case) in 2020. In 2020, EBF sustainably managed 430,000 Ha of land, compared to a target of 65,000 Ha set forth in the business case, surpassing the target by 561.5%. Compared to the 261,000 Ha recorded in 2019, EBF's Hectares of land under sustainable management increased by 64.8% in 2020. However, the fund has not met its water saving target for the last two years. In 2019 the total was 4.2m against a target of 6m (m3) and in 2020 the total was 4.5m against a target of 7.5m (m3).

The Fund is on track to meet its 1:2 leverage potential target in the private sector.

EBF continued to utilise drones and satellite imaging in 2020 to make more efficient and informed financial decisions that took environmental risk into account. Along with the EBF LAC fund, the development facility has steadily improved and expanded over the course of 2020, with a greater focus on technical assistance projects that use more efficient methods to promote sustainable agricultural practices.

**Effectiveness:**

As of 2020’s logframe results, EBF has exceeded all expected ICF KPI targets, and the majority of other indicator targets demonstrating effective progress towards the programme’s expected end of project goals. 430,000 Ha of sustainably managed land has been maintained by EBF to date, which far exceeded Defra’s 2020 target of 250,000 Ha. As of Q4 2020, the amount of new investment totals to $152.5 USD with the greatest number of new investments being approved in 2020 at 153. From this we can see that the project is demonstrating very good effectiveness at achieving the intended impact from outputs.

There is further work necessary in order to assesses the overall effectiveness of the fund in driving positive impacts for biodiversity. Targeted work and an external evaluation of the fund would help to address this.

**Equity:**

Equity signifies the extent to which benefits from programme spending reach disadvantaged and marginalised groups. Depending on context these groups may include women, disabled people, or specific ethnic groups. Given the Fund's focus on the use of intermediaries, there is limited data on downstream borrowers of relevance to equity considerations. However, some broad equity impacts may be inferred.

Fund progress towards its environmental outcomes has been strong over the last year. By the end of 2020, as a result of Fund activities, 1 million tons of CO2 were stored through agroforestry activities, 4.5 million m3 of water were saved, 430,000 hectares of farmland were brought under sustainable management, and 37,000 litres of herbicide use was avoided. Since the poorest and most marginalised in society tend to be heavily dependent on natural resources for their subsistence, and are most vulnerable to the impacts of climate change, a more resilient natural environment as a result of Fund interventions is likely to have equity benefits for marginalised groups.

Investments over the last year have also seen a significant increase in the number of borrowers supported through financial institutions focused on SMEs. Given that SME finance support focuses on businesses in which women are better represented as workers, business leaders, and agricultural holders, it is likely that this may have resulted in equity benefits.

The Development Facility has reached 394,000 individuals through events and training activities. Activities supported through this mechanism have included the development and implementation of Environmental and Social Management Systems (ESMS) for 12 partner institutions, and the recently launched 'Sustainability Academy' which aims to build capacity among the fund’s target audience and wider public. By building capacity, raising awareness and introducing a specific focus on social benefits within partner institutions it is likely that DF activities are having a positive effect on equity amongst stakeholders. However, as with the previous examples, data are not currently collected that enables these potential benefits to be tracked, measured and reported.

A wider review and update of logframe targets is planned. The Fund is also developing a gender strategy. Defra considers that as part of this it would be helpful to consider the inclusion of indicators specifically capturing benefits on gender, equity and social inclusion, to ensure these issues are monitored and can be reported on in future annual reviews.

**Coronavirus**

2020 was a challenging yet successful year for the EBF, as the Fund faced a difficult and deteriorating operating environment against the backdrop of COVID-19. Since early-March 2020, in response to the pandemic, the Fund’s Advisor activated a range of crisis-response measures to ensure adequate business continuity and to streamline its decision-making process to support the Fund’s target groups and its PIs while protecting investor interests. The investment priority of the Fund in 2020 was to provide funding to existing PIs that had a solid credit profile, needed additional liquidity and were key to the markets where they operate. Eight partner institutions of the EBF received a COVID-19 response package from the DF, which was designed to aid each bank in managing the operational challenges and react to the effects of the pandemic in a swift and sustainable way to strengthen and stabilise the funding base for sustainable business practices.

The financial performance of all counterparties of the Fund was reviewed and assessed for signs of increase in credit risk. As of 31st of December 2020, there was no deterioration in the portfolio of the Fund. As of date of reporting of the financial statements, the Fund has granted no loan moratoria and has not restructured any existing investments in 2020. In addition, all Fund counterparties have paid their contractual obligations. The shareholders, Board, Investment Committee, and relevant Service Providers to the Fund are regularly following the operating environment developments and the performance of all investments, and a special working group composed of members of the Board was established during 2020 to closely oversee these developments. The COVID-19 outbreak has not impeded the Fund’s ability to operate on an ongoing concern basis.

**Progress on recommendations from the previous AR, lessons learned this year and recommendations for the year ahead**

The recommendations from the 2019 annual review and progress on the recommendations is set out below:

1. Review if Defra should be providing more finance to the EBF: As Junior finance (such as Defra) continues to effectively leverage significant amounts of private sector finance, review the extent to which further Defra intervention could be utilised.

The programme performed well in 2019 and received an A in the annual review. Based on the continued success of the Fund since Defra’s initial £20m investment in 2016, Defra made a further investment of £12.6m in December 2019 to enable further leverage of private finance. Opportunities for further investment in EBF Africa were explored towards the end of 2020 but not pursued at this stage.

1. Consider how we work closer with other Donors: Particularly that of Junior investors (Germany and the European Commission) to increase fundraising and to raise ambition of the fund’s activities – both increasing private finance and sharing lessons for creating a viable investment model created by the EBF.

Defra continue to openly engage with other investors and the fund as an observer on the Board of Directors and as part of the Development Facility Committee, including providing feedback on new proposals and reviewing the effectiveness of ongoing or closed projects.

1. Update the Private and Public finance leveraged targets: As the methodology for calculating leveraged Public and Private finance has been updated, the targets are no longer suitable – these should be updated to reflect this change in 2020 Annual review.

This recommendation will be completed as part of a wider review and update of logframe targets in 2021/22.

1. A broader evaluation of the effectiveness of the EBF should be conducted: Defra’s objectives to a) increasing the amount of finance available for environmentally sustainable businesses and b) to embed the principles of green investment within the financial industry in relation to Land-Use investments (particularly Agriculture), by aligning financial incentives with environmental protection. From experience working with the EBF-Development Facility (where Defra sits as an observer) the EBF contributes significantly to this transformational change, a formal study would define this further and inform future investment decisions.

Defra is seeking to confirm funding and delivery for an external evaluation by the end of 2022, and has acquired funding to conduct a study into biodiversity indicators applicable to impact investment funds in 2021/22.

**D: RISK**

Risks here are specifically associated with risk to the EBF and its impact. Defra related risks (i.e., project management) undergo regular assessment internally.

Risks associated with impact and reaching milestones has been described in each output section. However overarching or notable risks have been summarised below.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Description of risk** | **Type** | **Risk rating** | **Likelihood** | **Mitigation activities** |
| Credit risk increase due to the sovereign debt crisis in Ecuador and the impact of the COVID-19 pandemic | Political and Economic stability | Major | Moderate | * Ecuador under intensive monitoring by EBF (country placed on Critical status) * Operating environment is weighting negatively on Ecuadorian credit risk: all PIs were placed on Watch and their internal ratings downgraded. EBF do not see the 2020 repayments as at risk * A PI made a regular repayment in Q2. EBF view the Ecuadorian PIs as well equipped to continue serving repayments coming due in 2020 * Ecuador successfully restructured its debt during Q3, whereby its sovereign rating was upgraded to B- by international rating agencies. The Advisor therefore moved the country out of the Critical monitoring category |
| COVID-19 negatively affected the economic outlook for all EBF countries in 2020; June IMF report forecasts a deeper GDP contraction for the region than initially projected in April | Political and Economic stability | Moderate | Low | * After having the entire portfolio under intensive monitoring for a quarter, no new material negative trends were identified – thus no new watch cases in Q2 2020 |
| Deteriorating macroeconomic environment with a deeper contraction than initially projected for 2020 due to COVID-19 and a slow recovery in 2021, especially in Colombia, Ecuador, and El Salvador | Political and Economic stability | Moderate | Low | * Regular monitoring of political and economic situation * Continued monitoring of loan repayments (so far loan repayments are as expected) * New investments, particularly in Guatemala and Honduras, have contributed towards reducing the portfolio concentration in top 3 countries (Colombia, Panama, Ecuador) |
| Nicaragua's sustained economic downturn since the political crisis that started in April 2018 was aggravated by the economic challenges driven by COVID-19 pandemic | Political and Economic stability | Moderate | Low | * Nicaragua remains on Watch since Q2 2019 * Regular monitoring of political and economic situation * Continued monitoring of loan repayments (so far loan repayments are as expected) |

**E: PROGRAMME MANAGEMENT:** **DELIVERY, COMMERCIAL & FINANCIAL PERFORMANCE**

**Finance:**

Defra has received the audited financial statement from EBF 1st January to 31st December 2020. The auditor’s report confirms that EBF’s financial statements give a true and fair view of the financial position of the Fund and of each of its sub-funds as of 31 December 2020, and of their financial performance and their cashflows for the year then ended in accordance with International Financial Reporting Standards (“IFRS”) as adopted by the European Union.

EBF LAC successfully attracted new funding into all instruments. During 2020, the Sub-Fund subscribed USD 73m Junior Shares, USD 12m Senior Shares, USD 32m Subordinated Notes and USD 21m Senior Notes. In 2020 the EBF LAC achieved distributions to holders of redeemable ordinary shares (i.e., Senior Shares) of USD 2.6 million, enabling the Sub- Fund to maintain pay-out of solid dividends for its Shareholders.

The total operating costs for 2020 comprised 1.7% of average total assets over 2020. A reduction, as a percentage of the Fund, from 2.81% in 2018 and 2.01% in 2019. Total operating costs include the Fund’s service provider fees, the cost of which has been covered directly from returns on investments of the Fund. The remaining income will be redistributed to the shareholders, via the income waterfall. The income waterfall will ensure that more senior debt and shareholdings are paid first before complementary dividends are paid to the Junior shareholders (Defra). As the Fund’s income has exceeded costs, Junior shareholders have received a dividend of 0.5% of their investment.

Defra’s investment in EBF continues to represent good VfM; significantly increasing the amount of funding available for financing environmentally sustainable business across Latin America and increasing its funding available to smaller businesses, exceeding the milestones set out by Defra and utilising its relationships with FIs to drive transformational change across the agricultural sector.

**Commercial:**

As of the end of 2019, 21 partner FIs and one Corporate have received financing from the EBF. In addition to the commercial contribution to FIs, the EBF continues to support the investment through TA delivered through the DF. DF activities throughout 2020 are described in detail throughout the review. As part of the work of the DF, EBF provides capacity building to FI staff - enhancing awareness and expertise in delivering finance to environmentally sustainable businesses. For example, TA has been provided in the form of various training programmes to over 600 staff from 19 PIs in 14 countries to increase financing of sustainable businesses.

**Reporting and monitoring:**

Throughout 2020 reporting timeliness and quality of reporting has been consistently good. Quarterly reports are sent to shareholders within 3 months of the quarter finishing, and the audited annual statement was provided within 3 months of the end of the year. The fund also produces an annual impact report. Defra is an observer on the Board of Directors and DF Committee. Meetings of the board take place every quarter and DF Committee meetings take place ad-hoc.

The evidence currently compiled by the Fund on the impacts of its investments or the information that is reported by partner institutions in the context of the bi-annual sub-loan reports is not disaggregated by sex or by age. To minimise the burden on the partner institutions, which is already significantly higher than for standard loans, the Fund does not intend to ask its partners to directly report this information. Instead, the Fund proposes to rely on third party evidence, when it is available, to provide estimates of gender disaggregation for certain indicators of interest. The EBF DF disaggregates sex in its monitoring and impact work. For outcome 1.7 (Number of jobs supported by sub-borrowers as a result of EBF support) in Defra’s logframe there is potential to focus in on the gender aspect of jobs supported, and Defra would be keen to discuss this with the Fund.

**Recommendation:** It is noted that EBF plan to develop a gender strategy for the fund to expand the work it has achieved to date and encompass additional strategies to address climate change by supporting female empowerment from a financial perspective. It is recommended that Defra work with EBF to help develop the gender strategy that is being developed.

The EBF’s continuous monitoring approach consists of the following activities:

1. Credit monitoring / monitoring of financial performance of investees

In 2020, the Fund Advisor followed its traditional credit monitoring approach consisting of quarterly risk reviews that are presented to the Rating Committee. The reviews were conducted for each PI and include a general review of performance in the recent quarter, spotting of trends, covenant monitoring and adjustment of ratings if necessary.

1. Monitoring of the use of proceeds (sub-loan monitoring)

PIs are required to report to the Fund Advisor on the use of Funds on a bi-annual basis. The Fund Advisor controls that its resources are used in the eligible sectors following the respective criteria and whether the partner institutions abide by the minimum required on-lending rate. Partner institutions report loan-by-loan on a specified set of information (such as loan amounts, target sector, financed activities, loan type, and sustainability standard and farm or business size) on an anonymous basis (no obligation to report names of sub-borrowers).

1. Monitoring through relationship management (visits, meetings)

As part of ensuring that its Funds are used according to its eligibility criteria, the Fund usually carries out regular visits to its sub-borrowers. However, due to the COVID-19 pandemic most visits were not able to take place. These visits were in part replaced with virtual meetings.

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| --- | --- | --- | --- |
| Date of last narrative financial report | Q4 2020 | Date of last audited annual statement | The 2020 annual statement has been audited, as of March 2021 |

**Evaluation of the Fund**

The fund has now been operational since 2014, and Defra’s investment has been active since December 2015 (with a further investment made in 2019). As set out in the business case and Annex 3 of the Subscription Agreement it is envisaged that regular external reviews of the Fund be carried out. An external evaluation (as stated in recommendation 4 in the 2019 annual review) would enable an objective review of the Fund to ensure it continues to meet Defra’s objectives of a) increasing the amount of finance available for environmentally sustainable businesses and b) embedding the principles of green investment within the financial industry in relation to Land-Use investments (particularly Agriculture), by aligning financial incentives with environmental protection. It would also be an opportunity to test the validity of the Fund’s theory of change, including for example uptake of environmental standards across FIs, effectiveness of green lists and standards with regards to climate and biodiversity impacts.

Defra has also defined a need for monitoring of biodiversity impacts across the portfolio. The Fund’s mission is to ‘promote business and consumption practices that contribute to biodiversity conservation, to the sustainable use of natural resources and to mitigate climate change and adapt to its impacts’, however there are currently no specific biodiversity indicators used by the Fund. Defra will be conducting work into biodiversity indicators applicable to impact investment funds investing in sustainable agriculture. Defra recommends that the Fund engage with Defra throughout this project and discuss ways to include findings within the Fund.

**Recommendations:**

1. Defra should undertake further work to consider best practice for impact investment funds in measuring biodiversity impacts, working with the fund managers and other industry practitioners.
2. Defra should undertake an external evaluation of the programme’s performance since initial investment, as referenced in the Annex 3 of the Subscription Agreement. The external evaluation should consider how the fund is progressing towards its outcomes and final impact through its activities and outputs.