

IDB GROUP PARIS ALIGNMENT IMPLEMENTATION APPROACH: PRINCIPLES, METHODOLOGY, AND TECHNICAL GUIDANCE

March 2023

This is a supporting document of the IDB Group Climate Change Action Plan 2021-2025 and contains technical or methodological advice to assist the integration of Paris Agreement alignment in operations and procedures.

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The team gratefully acknowledges the comments and inputs received from Amy Lewis, Maricarmen Esquivel, Alfred Grunwaldt, Adrien Vogt-Schilb, Raúl Delgado, Juliana Almeida, and Claudia Hernández (CSD/CCS), Veronica Adler (CSD/HUD), and Juan Carlos Paez Zamora (DSP/SEG).

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CONTENTS

EXECUTIVE SUMMARY

I.	Introduction: A Process to Support the Climate Transition.....	1
II.	IDB Group PA Alignment Implementation Approach for Operations	4
	A. The Need for an IDB Group Approach for PA Alignment in Operations	4
	B. Definition and Scope	5
	C. Key Principles of the IDB Group’s PAIA	14
III.	Conclusion: Enabling Conditions for Successful Implementation.....	16
	A. IDB Group: Institutionalization, Communications, and Capacity Building.....	16
	B. IDB Enabling Conditions	18
	C. IDB Invest Enabling Conditions	19
	D. IDB Lab Enabling Conditions	20
	E. Next steps	20
	Appendix 1: Activities Considered Universally Aligned to Mitigation Goals of the PA	21
	Appendix 2: Activities Considered Universally Not Aligned to Mitigation Goals of the PA	24
	GLOSSARY	25
	REFERENCES	28

ABBREVIATIONS

CC	Climate Change
CCAP	IDB Group Climate Change Action Plan
CCS	Climate Change Division
CO ₂ ^e	Carbon Dioxide equivalent
COP	Conference of the Parties
CRF	Corporate Results Framework
CS	Country Strategies
CSD	Climate Change and Sustainability Department
ERM	Eligibility Review Meeting
ESG	Environmental and Social Solutions Unit
ESPF	Environmental and Social Policy Framework
ESR	Environmental and Social Risk Management Unit
ESRS	Environmental and Social Review Summary
ESSP	Environmental and Social Sustainability Policy
FI	Financial Intermediaries
GDP	Gross Domestic Product
GHG	Greenhouse Gases
IDB Group	Inter-American Development Bank Group
IDFC	International Development Finance Club
IPCC	Intergovernmental Panel on Climate Change
LAC	Latin America and the Caribbean
LTS	Long-Term Strategies
MDB	Multilateral Development Bank
NDC	Nationally Determined Contributions
PA	Paris Agreement
PAIA	Paris Alignment Implementation Approach for operations
PBL	Policy-Based Loan
RMG	Office of Risk Management
SDGs	Sustainable Development Goals
UNFCCC	United Nations Framework Convention on Climate Change
VPC	Vice-Presidency for Countries
VPS	Vice-Presidency for Sectors and Knowledge

EXECUTIVE SUMMARY

IDB GROUP PARIS ALIGNMENT IMPLEMENTATION APPROACH: PRINCIPLES, METHODOLOGY AND TECHNICAL GUIDANCE

The IDB Group Climate Change Action Plan 2021-2025 (GN-2848-9) contains the actions to support the Latin America and the Caribbean (LAC) region's need for low-carbon and climate-resilient development finance and its plan to raise climate ambition continuously in the region. The plan centers on maintaining ambitious climate action by presenting key priorities at the IDB Group and regional level. Aligning the IDB Group financing to the Paris Agreement (PA) is one of the actions contemplated in the IDB Group Climate Change Action Plan 2021-2025 (Section III.A.2).

In support and preparation for this action, the "Paris Alignment Implementation Approach" (PAIA) is proposed as an analytical tool that encompasses a set of principles, a methodology, and technical guidance for project teams to assess, during project preparation, the alignment of new operations with the mitigation and adaptation goals of the PA. The PAIA is based on the principles of the "Joint MDB Assessment Framework for Paris Alignment for Direct Investment Operations", whose criteria assess whether finance can be considered not to undermine countries' transition to long-term carbon neutrality and climate-resilient development pathways in line with the PA. Therefore, this PAIA is the bespoke application of the Multilateral Development Banks (MDB) technical framework to operations at the IDB Group, given the business model and operational procedures of each of the IDB Group institutions.

IDB Group Management will apply the PAIA to all new operations that reached eligibility (with an approved Project Profile in the case of IDB operations and the eligibility confirmation in the case of IDB Invest operations) as of January 1st, 2023. The scope of the PAIA's application covers all investment loans, policy-based loans, guarantees, equity, investment grants with an approved amount greater than US\$3 million, and long-term corporate finance. Consistent with practice at other MDBs, the PAIA does not cover technical assistance or short-term financial instruments and does not apply to credit facilities for natural disasters and public health emergencies, nor to special development loans. Fee-based advisory and knowledge services are also not covered by the PAIA.

The application of this PAIA on operations is a client-centred process to ensure new financial flows provided by the IDB Group are compatible with the objectives of the PA. This process is grounded on national circumstances and considers the development pathway each country has defined to fulfill its commitments under the PA. For these purposes, PA alignment of IDB Group operations is considered and assessed within the broader goal of improving lives by reducing poverty and inequality in LAC, achieving development in a sustainable, climate-friendly way. The PAIA acknowledges ownership by countries and clients is key for successful climate action; therefore, it seeks not to exclude projects, but rather to identify opportunities to add value to countries and clients by supporting them in the transition to meet countries' climate commitments under the PA.

At a project-specific level, to assess the alignment of operations with the mitigation goals of the PA, the PAIA verifies that no activity is considered to undermine the transition to long-term carbon neutrality, ensuring that any risks of carbon lock-in and/or stranded assets are identified and managed. This assessment takes into consideration widely accepted decarbonization pathways in the global literature and practice; while acknowledging that institutional capacities and national realities, both in the private and public sectors, vary widely across the region. For this reason, the assessment will consider national priorities, as reflected in each country's nationally determined contribution (NDC) and long-term strategy (LTS).

The assessment of an operation's alignment with the adaptation goals of the PA leverages existing procedures under the IDB's Environmental and Social Policy Framework (ESPF) and IDB Invest's Environmental and Social Sustainability Policy (ESSP) to ensure physical climate-related risks relevant to the operation are identified and managed. Additionally, the IDB Group will reinforce mainstreaming efforts to ensure all targeted operations consider national and local priorities for climate adaptation. The application of PAIA will foster climate resilience as an outcome of IDB Group's operations whenever possible.

In using the PAIA, Management will aim to balance additional documentation disclosure and ongoing efforts at IDB Group to increase the efficiency of operational procedures, bearing in mind that enhanced disclosure of climate risks and opportunities is a mounting expectation from stakeholders. Documentation will help sustain and possibly increase access to concessional resources, as PA Alignment of operations becomes an access criterion to third-party resources.

The use of the PAIA is expected to have benefits both at the project level and in the dialogue with countries and clients. In operations, this approach will synergize with processes under IDB Group's environmental and social policies and climate mainstreaming efforts, enhancing the provision of innovative solutions to address development needs. Governments and private sector clients will be further supported in managing the effects of a warming climate and the financial opportunities of the transition to long-term carbon neutrality and climate-resilient economies. From a broader perspective, lessons learned from the use of PAIA will be fed back to sector guidance, policy support, technical assistance, market development, and country strategies (CS). This learning cycle will help the IDB Group build a strong dialogue and pipeline to assist countries and clients in addressing development priorities in ways that are consistent with countries' commitments under the PA.

This PAIA has been developed with the aim to guide the application of PA alignment assessments during its initial phase of implementation in 2023, promoting technical accuracy, consistency, and accountability. It has been designed with embedded flexibility to stay relevant within the context of national differences, evolving knowledge, and the learned experience from MDBs in the application of their joint technical framework. The PAIA will be revisited by Management within one year of its approval and updated as necessary. The approved PAIA will be distributed to the Boards of Executive Directors for information.

I. Introduction: A Process to Support the Climate Transition

- 1.1 **The achievement of social and economic development in Latin American and the Caribbean (LAC) is inexorably linked to the region's response to climate change.** Both the Inter-American Development Bank Group's (IDB Group) [Second Update to the Institutional Strategy](#), and its [Corporate Results Framework](#) (CRF) acknowledge this link and the challenges and opportunities it represents. The region is already experiencing the physical impacts of climate change at higher rates than the global average in terms of precipitation, mounting drought duration, temperature increase, and sea level rise, causing shorelines to retreat –particularly in small islands (IPCC, 2022). LAC is also exposed to the risk of stranded assets and losses in competitiveness, linked to market shifts away from assets that are intensive in greenhouse gases (GHG), which are increasingly acknowledged as essential to limit global warming to between 1.5 and 2.0°C as established in the PA. These impacts and shifts make the transition to climate-resilient and decarbonized economies a development priority.
- 1.2 **LAC is already reaping the benefits of transitioning to decarbonized and climate-resilient economies.** An example is the increase in foreign financing through sustainability-linked bonds, such as those in the [Green Bond Transparency Platform](#), which has already issued US\$33.5 B for a total of almost 28 M tCO₂ avoided or reduced (Delgado, 2021) (Conde, 2021). Another example is increased economic activity in coastal areas protected from climate risks, such as those seen in Barbados, where this type of investments boosted local GDP by more than 10% (Corral and Schling 2017). Growing flows towards sustainable projects are symptomatic of the major wave of innovation triggered by low-carbon technologies (Stern, 2012) and practices to bolster climate adaptation. The governments and businesses ready to harness this transition, stand to gain access to more efficient, secure, and affordable energy bases, cleaner and safer cities, greater access to markets, improved biodiversity, and better lives for people. By enabling the transition to sustainable development consistent with the goals of the PA, the LAC region can avoid stranded assets,¹ mitigate financial risks, and attract catalytic flows of investment: at least US\$35 trillion in sustainable assets that are expected to keep growing exponentially (GSIA, 2021).
- 1.3 **Tackling climate change by aiming for long-term carbon neutrality requires a specific focus on a just transition.** Decarbonization must happen leaving no one behind in the implementation of the Sustainable Development Goals (SDGs). Although getting LAC to net-zero and climate resilient economies is expected to generate 15 million net new jobs in the region and an estimated 1% of additional economic growth by 2030, employment and economic opportunities will change differently across sectors (Saget, Vogt-Schilb, & Luu, 2020). To ensure an equitable transition, it is necessary for countries and clients to plan today with an understanding of how costs and benefits are likely to be distributed across regions, economic sectors, and population groups. These insights must inform investments and solutions that address the needs of communities disproportionately affected. A just transition will manage economic adjustments with social equity, protect and increase the value of ecosystems, and ensure governments and businesses in LAC are able to harness opportunities to innovate and close investment gaps (Galindo & Vogt-Schilb, 2022).

¹ According to estimates specific for the LAC region, the failure to act on a timely manner to address the economic and technological shifts of the climate transition, can result in US\$90 billion worth of stranded assets in the power sector alone (Binsted et al., 2020) and approximately 9% of the regional GDP (Krishnan et al., 2022).

- 1.4 **Support for the climate transition must also respond to the dire social, fiscal, and economic impacts of the COVID-19 shock and the repercussions of the Russian war on Ukraine.** Due to the pandemic, during 2020 LAC faced a 7.4% fall in the regional GDP a 14% loss in investment, and an increase of 25 million people living in poverty, reaching 206 million in a single year. Overall, these impacts represent at least a ten-year setback in poverty and inequality reduction (IDB, 2022). This is compounded by the effects of the Russian war on Ukraine: alterations in the supply chains and trade flows of fossil fuel and agricultural products threaten food security² and could generate problems in the short-term balance of payments (Paolo & Michalczewsky, 2022). These events threaten development, but also demonstrate the increasing volatility associated to fossil fuels and signal a re-structuring of the economy: a global call for resilient and sustainable value chains in critical sectors such as food and energy production.
- 1.5 **The region is already committed to the goals and objectives of the PA.** All 26 of the IDB Group's borrowing member countries have ratified the PA, signaling the region's resolve to pursue the mitigation and adaptation goals and objectives of the agreement. Through Nationally Determined Contributions (NDCs), National Adaptation Communications, and Long-Term Strategies (LTSs),³ LAC countries are set to transition towards carbon-neutral and climate resilient economies. As the partner of choice in spearheading climate action in the region, the IDB Group is prepared to assist member countries and clients with these commitments, helping them improve and implement their plans until they are aligned with the long-term goals of the PA.
- 1.6 **In this context, the IDB Group will support the LAC Region achieve the goals of the PA and further promote sustainable and inclusive growth.** To ensure the LAC region remains competitive in the 21st century economy, it will be critical to consider how low-carbon and climate-resilient models help avoid loss and boost long-run Gross Domestic Product (OECD, 2017).⁴ A smart economic recovery will be one that aligns investments to the following three objectives of the PA, as stated in Article 2, without compromising food security nor the achievement of other SDGs:
- (i) Holding the increase in the global average temperature to well below 2°C above pre-industrial levels and pursuing efforts to limit the temperature increase to 1.5°C recognizing this would significantly reduce the risks and impacts of climate change.
 - (ii) Increasing the ability to adapt to the adverse impacts of climate change and foster climate resilience and low greenhouse gas emissions development, in a manner that does not threaten food production.

² Crop climate change modelling suggests rising risks to maize, soybean, and wheat production in LAC by 2050 (Fernandes, 2012). Due to the Russian war on Ukraine, the LAC countries most likely to be affected are net importers such as Jamaica, Barbados, El Salvador, Belize, the Dominican Republic, Surinam, Bahamas, Honduras (Paolo, 2022).

³ As stated in Article 4.19 of the Paris Agreement, LTS refer to "long-term low GHG emissions development strategies". Nonetheless, this document takes a broader approach to understanding country-led LTS as pathways to achieve a whole-of-society transformation, providing a link between the shorter-term NDCs and the long-term objectives of the PA, which includes long-term outcomes for climate adaptation and resilience (WRI, 2021).

⁴ Estimates, by the IDB, show an orderly transition will boost Chile's GDP by 5% and create net gains of US\$140 billion and US\$41 billion in Costa Rica by 2050. See (Benavides, et al., 2021), (Groves, et al., 2020) and (Quirós-Tortós & Godínez-Zamora, 2021).

(iii) *Making finance flows consistent with a pathway towards low greenhouse gas emissions and climate-resilient development.*

- 1.7 **In response to the request by borrowing member countries to have the Bank’s continued support in achieving their commitments under the PA, aligning IDB Group financing to the PA is a proposed action of the [IDB Group Climate Change Action Plan 2021-2025](#) (CCAP) (GN-2848-9).⁵ The CCAP set a series of actions to promote the “consistency of all financial flows with low carbon and climate-resilient development” and to “integrate PA alignment into IDB and IDB Invest operations procedures”. These actions are consistent with requirements in the [Environmental and Social Policy Framework \(ESPF\)](#), and IDB Invest’s [Environmental and Social Sustainability Policy \(ESSP\)](#). In turn, these rely on the [Disaster and Climate Change Risk Assessment \(DCCRA\)](#) and the [Climate Risk Assessment \(CRA\)](#) methodologies to systematically identify and manage climate-related physical risks. Actions on PA alignment also build on achievements through the [Sustainable Infrastructure Platform](#), and [NDC Invest](#). Finally, they are consistent with the [Bahamas Resolution](#), which welcomed Management’s objective to improve the evaluation of climate risks and to identify opportunities for resilience and adaptation measures at the project concept stage.**
- 1.8 **The proposal to align operations with the PA reflects the climate leadership of the IDB Group.** It is also consistent with commitments made by other major Multilateral Development Banks (MDBs).⁶ MDBs are in the process of incorporating PA Alignment in their operations according to their own policies and procedures, which in most cases have included an approval of the PA alignment methodology by their Management.⁷
- 1.9 **To support these actions and proposed reforms, the development and roll-out of the Paris Agreement Alignment Implementation Approach (PAIA) in all new operations is proposed to be applied as of January 2023,** in accordance with the indicative timeline included in document CA-604 (¶ 4.9).
- 1.10 **This PAIA establishes a methodology, set of principles and technical guidance to assess alignment to the PA during its initial implementation phase in 2023.** Methodical steps and key principles delineated in this document seek to guide the PA assessment in a manner that provides consistency, comparability, and technical rigor. The IDB Group also acknowledges that the method to assess PA alignment is still evolving, and further definition will be gained as it is applied in a larger set of projects. To ensure

⁵ The CCAP was discussed at the IDB’s Policy and Evaluation Committee and IDB Invest’s Committee of the Board and then approved by Management of the IDB Group (December, 2020).

⁶ In December 2017, at the One Planet Summit, Multilateral Development Banks (MDBs) including the IDB Group - and the International Development Finance Club (IDFC) committed to work together on Article 2.c of the PA. The African Development Bank (AfDB) committed to fully aligning new operations to the PA by the end of 2023, and all its activities by the end of 2025. Asian Development Bank (ADB) committed to achieve full alignment of sovereign operations by July 2023 (non-sovereign operations will reach 85% by 1 July 2023 and 100% by 1 July 2025). The Asian Infrastructure Investment Bank (AIIB) will align its operations with the PA by July 2023. The European Bank for Reconstruction and Development (EBRD) will align all its activities by the end of 2022. The European Investment Bank (EIB) Group aligned all new projects and operations with the goals of the PA since the beginning of 2021. The Islamic Development Bank (IsDB) will fully align its activities by the end of 2023. The World Bank Group (WBG) will align all new operations starting July 1, 2023 (private sector arms, IFC and MIGA, 85 percent of Board approved real sector operations will be aligned starting July 1, 2023, and all operations starting July 1, 2025).

⁷ Such is the case of the AfDB, the ADB, and the WBG, for example.

learning, the PAIA will be revisited by Management within one year of its approval and updated as necessary. The need for updates will be assessed, based on: (i) updated by MDBs to the principles of the [“Joint MDB Assessment Framework for Paris Alignment for Direct Investment Operations”](#) lessons from the initial application of the framework (including those by other MDBs); (ii) external developments and scientific advancements that may modify reference values and/or technical definitions; and (iii) insights on the social, policy, and markets shifts and technological uptake in LAC, including the evolving frameworks used to disclose climate risks in the context of development projects.

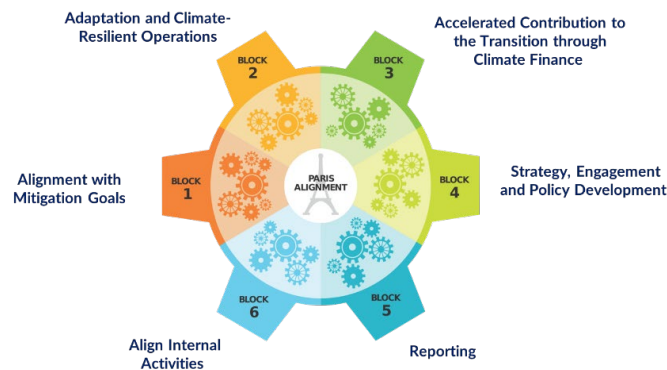
- 1.11 **The structure of the document is as follows:** Part I presented the purpose of this document (the PAIA) and the motivation for assessing the PA alignment of all new IDB Group operations as of January 2023. Part II defines key terms and scope for the PAIA, based on the technical framework for assessing alignment of direct investment operations, and establishes the key principles that will guide its application at IDB Group. Part III concludes by laying out a set of recommendations to address key challenges going forward and facilitate the implementation of the PAIA.

II. IDB Group PA Alignment Implementation Approach for Operations

A. The Need for an IDB Group Approach for PA Alignment in Operations

- 2.1 **To help countries meet their commitments under the PA, the MDB Climate Change Working Group⁸ agreed on six building blocks to align financial flows with the goals of the PA.** At the One Planet Summit 2017, the IDB Group, along with other MDBs and the International Development Finance Club (IDFC), [announced their intention to align their financial flows with the goals of the PA](#). In a [joint declaration in December 2018](#), MDBs outlined six building blocks (BB) for achieving full PA alignment (see Figure 1).

Figure 1. MDBs Paris Alignment Building Blocks



- 2.2 **As part of the approach, MDBs have adopted a methodological approach to assess the PA alignment of operations.** To advance in the implementation of the first two building blocks of their overall approach (BB1 and BB2), at COP26 in Glasgow MDBs adopted the [“Joint MDB Assessment Framework for PA Alignment for Direct Investments”](#) (see Figure 2). Based on its essential principles and criteria, MDBs further developed

⁸ Constituted by members of the AfDB, ADB, AIIB, CEB, EBRD, EIB, IDBG, IsDB, NDB, and WBG.

frameworks for policy-based operations, intermediated finance,⁹ and general corporate purpose finance¹⁰ (see [Figure 3](#)). In 2022, these methodologies were consolidated for the publication: “Joint MDB Methodological Approach for Assessment of PA Alignment.”¹¹

2.3 **The IDB Group operationalization of the principles in the “[Joint MDB Assessment Framework for Paris Alignment for Direct Investment Operations](#)” and complementary frameworks for other financial instruments require adaptation and interpretation according to the mandates and policies of each of the corresponding IDB Group’s institutions.** A harmonized approach for IDB Group is essential for providing clear and consistent support to countries and clients across sectors and funding instruments, based on its pipeline and tools.

2.4 **This document is a guide for IDB Group personnel in charge of preparing operations.** Main strategic audiences include country representatives, country economists, division chiefs, personnel working on development effectiveness, strategy, and programming. Main operational audiences cover chiefs of operation, country coordinators, project teams, investment officers, environmental and social risk management specialists, and others seeking to ensure alignment of operations with the goals of the PA as they move from programming to design.

B. Definition and Scope

2.5 **The assessment of operations’ alignment with the PA is based on the principles in the “Joint MDB Assessment Framework for Paris Alignment for Direct Investment Operations” (¶2.3).**¹² The IDB Group collaborated with other MDBs in an assessment framework that requires alignment to mitigation *and* to adaptation objectives in *all* components of a given operation (see [Figure 2](#)). These frameworks characterize projects as either “aligned” or “not-aligned,” allowing no conditionalities or values in between.

2.6 **Alignment with the mitigation objectives of the PA involves ensuring operations present no inconsistencies with country-owned plans for low-GHG emissions and that they do not undermine the transition to net long-term carbon neutrality**¹³ **economies, in that country and globally.** In the technical framework for assessing alignment of direct investment operations for direct investments, a two-pronged assessment first applies a screening to identify investments considered “universally

⁹ This methodology covers financing delivered through banks, non-banking financial institutions, leasing companies, funds and other financial intermediaries.

¹⁰ This methodology covers direct real sector investment operations without targeted use of proceeds and an approach focused on the counterparty alignment. It covers in particular: working capital, revolving credit facilities, trade finance through a corporate, supply chain finance with a corporate anchor company, equity investments for corporates, general guarantees which do not specify coverage to specific activities or assets.

¹¹ Expected to be made public in 2023.

¹² The use of such a framework was anticipated in the CCAP 2021-2025 and in the document CA-604 (“Climate Change and Sustainability. Working Group 6”).

¹³ This follows the IDB ESPF which acknowledges that long-term carbon neutrality is necessary to confront climate change and steer economic development toward a more sustainable, resilient, inclusive, and competitive future.

aligned”¹⁴ or “universally not aligned”¹⁵ to mitigation objectives in the PA (see Appendix 1 and 2). After this uniform assessment, projects that do not fall under either category, must be assessed vis-à-vis specific criteria to ensure they: (i) do not contradict country-owned NDCs, LTSs, or global sector-specific pathways towards decarbonization, considering the specific context and the principle of common but differentiated responsibilities;¹⁶ (ii) do not “lock-in”¹⁷ GHG emissions levels that are inconsistent with long-term carbon neutrality, by ensuring all technically and financially feasible lower-GHG solutions are assessed considering a long-term view of how they will continue to operate; and (iii) when applicable, include strategies to manage climate transition risks that may jeopardize the economic viability of the investment and/or result in stranded assets for the country or client. It is important to underscore these criteria must be met and analyzed given the best available information,¹⁸ considering the national context and differentiated capacities of clients and partners. The same spirit is carried to the joint MDB technical assessment frameworks for other types of finance, as captured in each specific methodology for PBLs, intermediated, and general corporate purpose finance.

- 2.7 **Alignment with adaptation objectives of the PA involves ensuring that operations identify and address physical climate risks, consider ways to build climate resilience, and present no inconsistencies with national/local priorities for climate adaptation.** In the Joint MDB technical framework for assessing alignment of direct investment operations for direct investments (those with known use of proceeds), this entails having a process in place to screen all investment operations for physical climate risks, and when applicable, incorporate measures to address those risks while fostering climate resilience in ways that are consistent with country-owned adaptation plans and priorities.¹⁹ The same spirit is carried to the assessment of other types of finance, as captured in each specific methodology for PBLs, intermediated and corporate finance. At the IDB Group, alignment with adaptation goals largely leverages existing procedures under the ESPF and IDB Invest’s ESSP.

¹⁴ For example: climate-positive investments such as generation of renewable energy, cleaner cooking technologies that substitute solid biomass fuels in open fires; conservation of natural habitats and ecosystems; electric mobility, etc. But also, climate neutral activities such as civic justice, gender, and education policies. See Appendix 1.

¹⁵ Presently, this list only includes extraction or electricity generation from coal and from peat. These types of investments are already excluded by the ESPF and the ESSP. See Appendix 2.

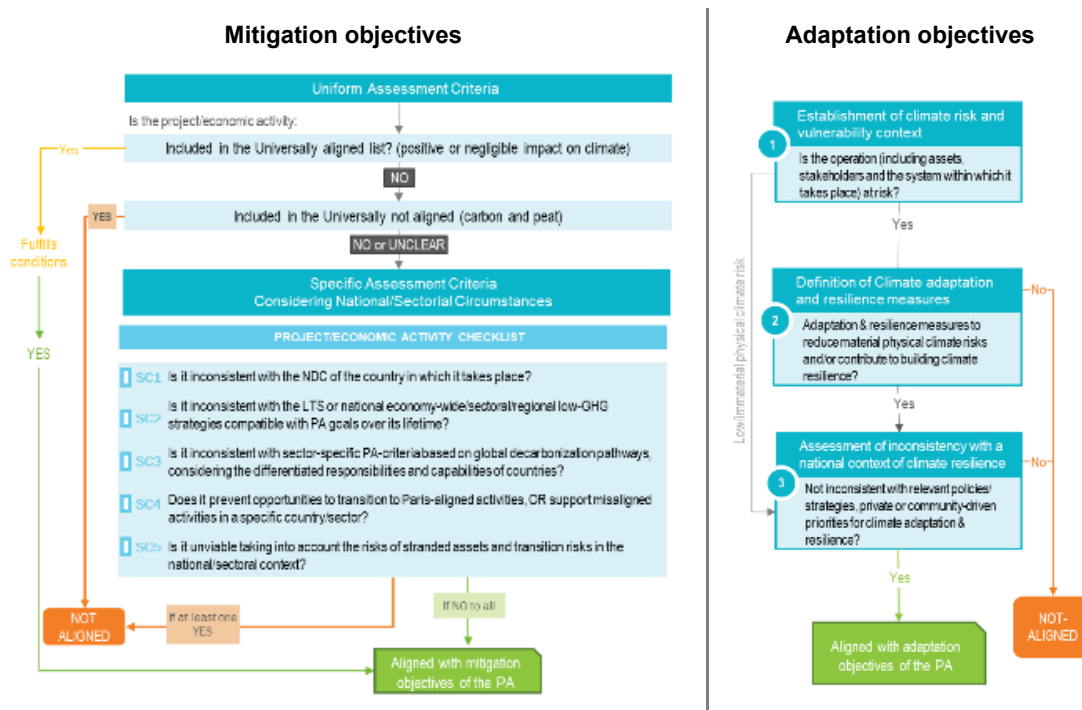
¹⁶ Common but Differentiated Responsibilities and Respective Capabilities is a principle within the United Nations Framework Convention on Climate Change (UNFCCC) that acknowledges the different capabilities and differing responsibilities of individual countries in addressing climate change.

¹⁷ This refers to the avoidance of “carbon lock-in”, which in practice entails analyzing any GHG-intensive asset financed by the IDB Group considering its emissions levels, expected lifetime of operation, and technically and economically feasible alternatives and/or arrangements that may replace it or reduce its emissions to net zero by mid-century. This also includes considering ways to avoid reinforcing market dynamics that set barriers for the transition, e.g., deter the entry of market players that offer lower GHG alternatives for this type of investment.

¹⁸ In some instances, information may not be available or be very limited; this will not lead to a non-alignment decision, but rather, the assessment will rely on the specific criteria for which information is available.

¹⁹ Specifically, for the IDB, the application of the DCCRA methodology as part of the ESPF addresses most of the analytical needs to verify this alignment in direct investments. For operations outside the scope of the ESPF, project preparation will identify relevant entry points to address climate vulnerability. All operations starting 2023 will ensure no inconsistencies with climate adaptation national plans and local priorities.

Figure 2. Decision Trees for Assessing Alignment of Direct Investments with Objectives of the PA



Source: Adapted from (MDB Group, 2021)

2.8 **The boundaries of the PA alignment assessment will consider the broader economic activity and a long-term view of climate impacts.** When determining alignment to mitigation and adaptation goals of the PA, the IDB Group will primarily rely on its definition of “area of influence” and relevant present and reasonably foreseeable developments associated to an operation as defined in the ESPF and ESSP.²⁰ Also, it will acknowledge that, “in some instances, the extent of assessment needs to take into account the broader economic activity in which the operation takes place”. For this, the IDB Group’s approach will be commensurate to risk (¶2.14) in determining when alignment with mitigation objectives should stress any of the following: (i) inputs; (ii) outputs (goods and services delivered by the operation);²¹ and (iii) regulations upon which viability of the operation depends (Joint MDB technical framework for assessing alignment of direct investment operations, ¶20). For adaptation, a similar approach will be used to consider

²⁰ The ESPF applies to operations at IDB and IDB Lab, while the ESSP is applicable to transactions from IDB Invest and will be complemented by the IDB Invest Operation Manual. Under the ESPF, the term “area of influence” encompasses: (i) the area likely to be affected by the project and the client’s activities and facilities that are directly owned, operated or managed, and that are a component of the project; (ii) impacts from unplanned but predictable developments caused by a project that may occur later or at a different location; or (iii) indirect project impacts on biodiversity or on ecosystem services upon which project-affected people’s livelihoods depend. It also includes associated facilities and cumulative impacts that result from the incremental impact of the project when added to impacts from other relevant past, present, and reasonably foreseeable developments as well as unplanned but predictable activities enabled by the project that may occur later or at a different location.

²¹ For example, a transportation operation where the development objective is to boost indicators for agricultural exports, will need to at least identify and document agriculture-related transition risks and climate vulnerabilities.

the need to account for the risk of increasing or shifting climate vulnerability beyond the project's temporal boundaries. Further analysis of these considerations (¶3.7) will allow to better inform the assessment of PA alignment.

- 2.9 **The alignment of an operation to the PA is distinct from climate finance accounted in it.** Since 2015, the IDB Group tracks contributions to the climate change agenda based on the MDB Joint Methodology of Climate Finance and reports them in the CRF under Strategic Alignment Indicators 3.5 and 3.6.²² This is distinct from alignment to the PA, which serves to demonstrate the consistency of financial flows with long-term carbon neutrality and climate-resilient development; a project can have no climate finance and still be aligned to the PA. Nonetheless, an operation that is not aligned to the PA cannot count for mitigation-related climate finance, as per the MDB Joint Methodology for Climate Finance.²³
- 2.10 **The application of PAIA will begin with new sovereign and non-sovereign guaranteed operations at IDB Group that reach eligibility as of January 1st, 2023.** The PAIA will be applied on all operations that reached their eligibility approval as of January 1st, 2023. The scope of application includes investment loans, policy-based loans, guarantees, equity, long-term corporate finance, and investment grants with an approved amount greater than US\$3 million.²⁴ New operations or projects reformulated under these lending types will follow the corresponding four different technical frameworks developed by MDBs: *direct investment*, *policy-based lending operations*, *intermediated financing* and *general corporate purpose finance* (see [Figure 3](#)). The PAIA will not be applied retroactively in operations that reached eligibility before the year of 2023. Specific guidelines containing the operationalization of the PAIA throughout the project cycle and among project teams will be established by IDB, IDB Invest, and IDB Lab in their own bespoke processes and workflows.²⁵
- 2.11 **Consistent with practice in other MDBs, PAIA does not apply to technical assistance or short-term financial instruments.** More precisely, PAIA does not cover technical cooperations, contingent credit facilities for natural disaster and public health emergencies (CCF), and Special Development Loans (SDL). It also does not cover short-term corporate loans, nor does it cover non-reimbursable investment grants with an approved amount less than or equal to US\$3 million. However, technical assistance will be subject to periodic revision and guidance as part of the upstream agenda to promote PA alignment of operations. Fee-based Advisory and Knowledge Services at the IDB are not covered by the PAIA.

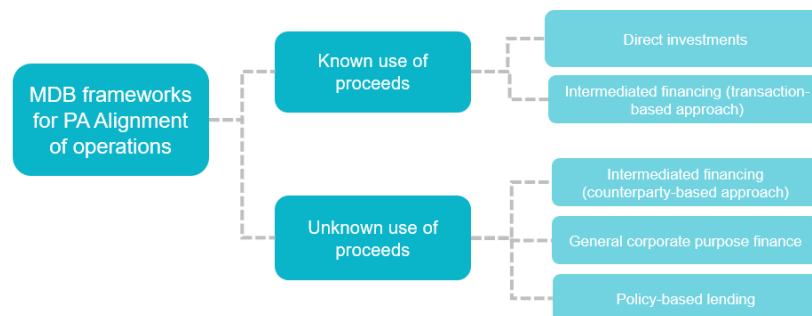
²² Indicator 3.5 Climate Finance in IDB Group operations (% of approved/committed amount) and Indicator 3.6 Projects supporting climate change mitigation and/or adaptation (% of approved of approvals/commitments).

²³ To be eligible for mitigation climate finance, activities should: “neither hamper the development and deployment of very-low-carbon alternatives nor lead to locking in carbon-intensive assets inconsistent with the long-term decarbonization goal.”

²⁴ Given the distinct nature of IDB Lab's portfolio, which is characterized by smaller transactions, the application of PAIA will aim to cover operations of all amounts. Given the possible implications for transaction costs the application will prioritize particularly those amounting to US\$500K and above.

²⁵ Each arm of the IDB Group will be developing arrangements for the integration of PA Alignment in their operations and procedures.

Figure 3. MDB Joint Frameworks for PA Alignment by type of instrument



- 2.12 **During its initial implementation phase, PAIA applies to all operations but prioritizes four sectors according to their PA needs, and proposes a dedicated approach for operations with intermediated finance.** ²⁶ In coordination with other MDBs and based on an analysis of IDB Group’s recent pipeline of operations (see [Box 1](#)), the IDB Group has identified certain sectors as a priority in terms of how much additional analytical guidance they require to assess their PA Alignment. This is the case of operations related to energy, transportation, water and sanitation, and agri-food systems, as well as IDB Group’s approach to PA alignment of operations with financial institutions. Additional analytical guidance for these sectors (see [Table 1](#)) has been initially discussed with representatives of Civil Society Organizations (CSOs),²⁷ and will continue to be discussed and updated as information on sector-specific pathways for decarbonization and climate resilience emerges. Also, as the PAIA continues to develop, additional sector guidance will follow, with considerations for high-emitting industries (aluminium, cement, and steel), buildings, and digitalization, among others deemed necessary to inform the assessment of PA alignment. It is important to note that such guidance will not aim to establish new exclusions outside of those already provided under existing policies at the IDB Group. Guidance documents will be approved by Management to be used by project teams.
- 2.13 **The expected implication of PAIA is a strengthening of the links between operations and the system-level policy and markets’ transitions encouraged by IDB Group through its country dialogue and financial products.** The systematic application of this framework will support project teams in the identification of key technical, policy, and market barriers and needs to support PA-aligned pathways (“climate transition gaps”). The outcome of the PA alignment analysis will allow better coordination between technical assistance, advisory services, financial products, and other donors and partners in the region to raise awareness, support piloting and scale-up of PA-aligned practices alongside financial returns and accelerate the transition towards decarbonized and climate-resilient

²⁶ Future iterations of the approach will include additional considerations for high-emitting industries (aluminum, cement, and steel), buildings, and digitalization, deemed necessary as a product of initial applications and learning.

²⁷ On September 21st 2022, the IDB Group carried out a “Dialogue on Paris Agreement Alignment” where technical specialists presented the main aspects of its approach to PA alignment to representatives of 34 CSOs. Inputs and feedback from the dialogue with CSOs were collected to inform this version of the PAIA.

economies. Like the ratchet mechanism of the PA, this will allow the IDB Group to increase the ambition and climate quality of operations over time.

Box 1. Implications of PA Alignment for operations at IDB Group

Each arm of the IDB Group carried out a baseline assessment to approximate the operational impact of applying the Joint MDB Framework for PA alignment. Main findings are summarized below.

IDB

In 2021, a revision of 2019 approvals at the IDB found that five of every six operations were already aligned with mitigation and adaptation objectives of the PA.²⁸ This suggests that existing processes at IDB, such as the application of the former safeguards policy and climate mainstreaming efforts, were already covering aspects of PA alignment. The remaining 16% of total approvals during the period were deemed to require further specific assessment and possibly perform adjustments to justify their alignment:

- (i) Carbon-intensive energy investments such as support for midstream and downstream activities in the fossil fuels sector (e.g., feasibility studies for LNG introduction, incentives for gas exports). This includes PBLs that support energy investment plans that include further fossil fuel development. Their PA alignment would have required a reference to countries' NDC, LTS (where existent) and science-based emissions trajectories presenting viable alternatives, to verify whether these investments could be deemed consistent with temperature goals of the PA given the country context.
- (ii) Activities that require additional information and activity elements to acknowledge and manage the risk of carbon lock-in and/or climate transition risks:
 - a. Direct support, or indirect support (e.g., through enabling infrastructure), for GHG-intensive activities (livestock, cement, timber, aquaculture intended for exports) that may have considered ways to support less GHG-intensive development models, and/or alternatives to address carbon lock-in.
 - b. Infrastructure investments with an impact on carbon stocks through direct loss of forest cover (all of which included a Biodiversity Plan in compliance with safeguards) or that present a risk of indirect land use change (ILUC). Particularly in contexts of weak land governance and rapid land use change, these may merit adjustments to ensure maintenance of carbon storage capacity, traceable sustainable resource management, and/or measures to strengthen land use controls.
 - c. Transportation projects that involve capacity expansion, particularly in contexts with high modal share trends that favor internal-combustion engine vehicles; these may require further contextualization within integrated strategies to support sustainable land use planning, low-carbon mobility and the overall decarbonization of transport.
 - d. Tourism and coastal development operations that may require more systemic assessment of long-term climate impacts and further clarity on their embeddedness in comprehensive country-owned climate resilience strategies.

Most operations assessed applied the Joint MDB direct investment methodology to determine PA alignment; 19% required the approach for PBLs; 8% qualified as operations channeling funds through financial institutions.

IDB Invest

End of June 2021, IDB Invest assessed all corporate, energy and infrastructure transactions in portfolio for alignment with the mitigation objectives of the PA.²⁹ The assessment found that two out of every three operations were likely aligned³⁰ with one third requiring more information to conduct the assessment. Of those operations requiring more information, one third (or approx. 11% of the full portfolio) was considered at high risk of inconsistency with the goals of the PA. Key conclusions from the assessment include:

²⁸ Of a total of 114 operations reviewed, 68% were already clearly aligned, 16% involved buildings and/or digitalization technologies that could have validated their alignment by stating commitments to energy efficiency standards and when possible, additional actions to facilitate the transition to low carbon trajectories.

²⁹ The analysis was carried out applying the Direct Finance MDB BB1 methodology to all transactions.

³⁰ Likely aligned means the transaction in its current form or with only minor alterations would be aligned.

- (i) Transactions at high risk of inconsistency with the goals of the PA include those in ruminant livestock, petrochemicals, midstream and downstream activities in the gas sector (including gas power plants and supporting infrastructure), transportation infrastructure and high-emitting industries such as cement and construction materials.
- (ii) The portfolio at large is diversified from a PA mitigation perspective as emission intensive and/or fossil fuel reliant projects in portfolio are spread across multiple sectors and industries.
- (iii) Assessment challenges and information gaps to determine mitigation alignment exist particularly in the areas of global sectoral decarbonization path alignment, carbon lock-in risk as well as transition and stranded asset risk. In some cases, building out existing workflows and equipping teams with adequate resources solves this challenge. This includes ensuring analysis of alternatives and carbon shadow pricing analyses are conducted for high-emitting projects. In other cases, additional information from the client, for instance on emission intensities and transition plans, is necessary to enable a full assessment.
- (iv) The Joint MDB methodology for real sector direct investments without targeted use of proceeds will play a key role in the operationalization of PA at IDB Invest. This is due to the significant proportion of transactions that include general purpose financing components such as working capital or supply chain finance. This is especially relevant for the industry and agribusiness portfolio.
- (v) The portfolio review confirmed both the need for a location- and context-specific PA analysis for adaptation and the synergies between the existing process for physical risk assessment and the PA analysis for adaptation.

Opportunities exist to scale up climate related technical assistance, in particularly to assist clients in developing Paris aligned decarbonization strategies and resilience measures.

IDB Lab

The analysis of IDB Lab's approvals during 2019 revealed that 83% of operations were clearly aligned to the objectives of the PA, while the remaining 17% of operations would have required to either present additional information or carry out limited adjustments to validate their alignment with the PA. Out of 89 projects assessed, 13.5% required the application of the methodology for intermediated finance.

The main areas where further analysis and validation were deemed necessary to validate PA alignment are general client support and those related to "knowledge economy" (in areas such as agricultural technologies and export markets) and "inclusive cities" (construction, waste management and other infrastructure). Main recommendations that stemmed from the analysis include: (i) further consideration of climate physical risks in economic viability analysis and incorporation of measures to build climate resilience whenever possible (even in operations with low physical climate risk); (ii) acknowledgement of transition risks associated to potential climate regulations, such as carbon pricing on exported goods, and also to technology shifts and changing consumer behaviors; and (iii) support end-beneficiaries with traceability measures to validate low-carbon content and adequate management of climate-related risks.

Table 1. Summary of Additional Technical Guidance Required to Assess PA Alignment in Key Sectors

	BB1 (PA Mitigation goals)		BB2 (PA Adaptation goals)
Sector	Activities considered universally aligned under BB1 per IDB Group's interpretation [1]:	Analytical elements and criteria to determine alignment under BB1 in projects that require a specific assessment, such as [2]:	Analytical elements to review alignment under BB2
Energy	<ul style="list-style-type: none"> • Generation of renewable energy; • Energy efficiency; • Green hydrogen; • Rehabilitation of existing hydropower plants; • Electricity transmission and distribution (including energy access); • Energy storage; • Cleaner cooking technologies; • Demand-side management investments. 	<ul style="list-style-type: none"> • Midstream and downstream investments related to oil and gas; • Construction of new hydropower plants with reservoir; • First generation biofuels; • Carbon capture, use and storage technologies or gas flaring reduction in fossil fuel projects; • Energy storage with reversible pumping or with hydrogen; • Non-green hydrogen; • Technologies with a significant reliance on fossil fuels and/or fossil fuel subsidies. 	<ul style="list-style-type: none"> • A review of key linkages between sector-specific investments and alignment with the long-term climate resilience goals of the PA; • Relationship between alignment to adaptation objectives of the PA in the sector, and IDB Group's existing environmental and sustainability policies to assess and address physical climate risks in operations; • Sectorial technical and institutional tools and frameworks to support mainstreaming resilience into operations and upstream planning and to prevent
Transport	<ul style="list-style-type: none"> • Electric and non-motorized urban mobility; • Low transit roads (which link rural and/or vulnerable populations to community services, or that link local products to consumer or export markets); • Short sea shipping, port and rail infrastructure that do not depend on fossil fuels; • Road works not related to capacity expansion. 	<ul style="list-style-type: none"> • Road upgrading with significant addition of lanes or that rely on short-term increase of traffic to be economically viable; • Other works that can be considered capacity expansion of roads; • Projects in the aviation sector; • Other transportation investments that significantly depend on fossil fuels. 	
Water and Sanitation	<ul style="list-style-type: none"> • Water treatment and effluent treatment; • Water supply networks and sewage systems; • Pumping stations that use renewable energy; • Rainwater harvesting, drought management; • Projects to conserve and restore ecosystems, control erosion and stabilize riverbanks; • Biogas; refuse-derived & solid recovered fuels; • Composting; drainage and stormwater. 	<ul style="list-style-type: none"> • Desalination plants; • Carbon-based pumping; • Construction of reservoirs; • New landfill capacity; • Incineration of urban solid waste and closure of dumping grounds. 	

	BB1 (PA Mitigation goals)		BB2 (PA Adaptation goals)
Sector	Activities considered universally aligned under BB1 per IDB Group’s interpretation [1]:	Analytical elements and criteria to determine alignment under BB1 in projects that require a specific assessment, such as [2]:	Analytical elements to review alignment under BB2
Agri-food sector	<ul style="list-style-type: none"> • Afforestation, reforestation, sustainable forest management, forest conservation and soil health improvement, including the recuperation of degraded lands or ecosystems; • Climate-smart agriculture and agroecology; • Conservation of natural habitats and ecosystems; • Sustainable fishing and aquaculture; • Efficiency in water management and/or use; • Water management at watershed level; • Irrigation systems with renewable energy. 	<p>Activities that cannot be considered universally aligned in the sector or whose justification for inclusion within said list is not validated.</p> <p>Project teams will pay particular attention to components and operations that promote the production of items that could be associated with high levels of GHG emissions such as livestock and flooded rice systems, or sectors with potential links to land use change. Also, those where the specific origin and destination of items can be identified, emissions linked to transportation will be considered.</p>	maladaptation-related risks.
Inter-mediated finance through financial institutions	<p>Definition of a parallel route to assess the PA alignment of the operations with financial intermediaries in LAC based on two pillars:</p> <ol style="list-style-type: none"> 1) Transaction-based alignment, which ensures that proceeds of IDB Operations are directed towards activities aligned with mitigation and adaptation goals of the PA, using sector guidance as a reference in operations within a sector characterized by non-negligible emissions or risk of carbon lock-in. 2) Counterparty-based approach, through which the IDB Group will continue to support FIs clients to build their capacities to align –over time and according to local context and available resources– their overall operations to the goals of the PA. 		

[1] Provided that the operation does not depend on the significant direct use of fossil fuels, nor its economic feasibility depends on the production, processing and/or transport of fossil fuels or on fossil fuel subsidies. For conciseness, this list has been summarized. The full MDB list is included in Appendix 1.

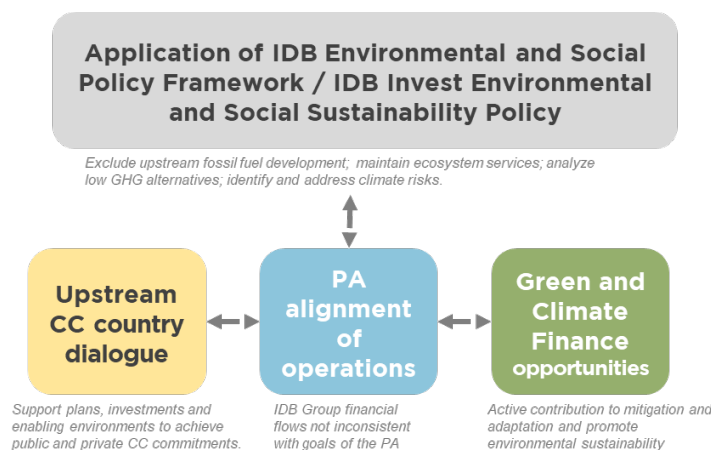
[2] These are indicative, non-exhaustive lists of types of projects that would require a specific assessment to validate alignment to the PA mitigation goals.

C. Key Principles of the IDB Group's PAIA

- 2.14 **A collaborative process with a focus on a just transition.** The main aim of this PAIA is to assist and enable the fulfillment of the commitments made by all our borrowing member countries when they signed the PA and submitted their NDCs, as recorded under the [UNFCCC Registry](#). The application of PAIA should not be interpreted as a judgement by the IDB Group of our partners' policies, plans, or other actions. The greatest value-add of implementing the PAIA is the engagement and support given to clients and operations during the collaboration that precedes any PA alignment assessment, beginning as early as Country Strategy and programming dialogues. To maximize positive synergies with all development needs, the application of PAIA to upstream dialogue and operations will seek a just transition: identify and address whether the costs and benefits associated to the low-carbon and climate-resilient transition are or not fairly distributed, guided by the MDB Just Transition High-Level Principles (MDB Working Group, 2020). Policy dialogue that stems from the identification of "climate transition gaps" (see ¶1.11, footnote 8) will seek to engage social development and labour markets specialists in finding models that address the distribution of costs and benefits from the low-carbon and climate-resilience transition.
- 2.15 **Opportunities to transition and risk mitigation measures consider equity and country-specific context.** The development needs of LAC countries and their financial and technical abilities to transition are varied and vast. This creates disparities regarding feasible rates of decarbonization and capabilities for building climate resilience. Emission levels in LAC are vastly different from those of other geographies aiming for PA alignment, such as Europe and the United States; even so, per capita levels of emissions in LAC are comparable to the total world average (6.2 ton CO₂^e) and loss of forests in the region have constituted the fifth largest CO₂^e source in the world (TNC, 2020). In this context, the IDB Group PAIA accounts for national differences, regional and urban priorities (e.g., preservation of carbon stocks and natural capital), and stresses the urgency of adaptation to climate impacts in LAC.
- 2.16 **Assessment efforts and technical support are commensurate to the operation's climate risk.** Operations that after an initial screening show no material risks of continuing fossil fuel reliance and/or GHG-intensive development (which includes ensuring no loss of high value carbon stocks, linked to the application of the ESPF and ESSP), and also present no material risk from physical impacts of climate change, will be deemed PA-aligned using a simplified assessment. A specific assessment for PA alignment will be reserved exclusively for projects that are not deemed universally aligned to the mitigation goals of the PA and/or that risk being contrary to national climate adaptation priorities.
- 2.17 **PA alignment contributions to programming and operational design decisions are timely.** Upstream policy dialogue and strategic selectivity are the driving forces for applying the PAIA, as they are the most effective way to shift financial flows at country and corporate level and focus on real world impact. As such, additional support be most timely during dialogue on strategy, programming, and identification. For this reason, the IDB Group is already supporting policy shifts, low-carbon, and climate-resilience strategies, and increasing in-country presence of climate specialists. Engagement with countries and clients regarding potential inconsistencies between proposed operations and the goals of the PA, will include a discussion on how the IDB Group can support the transition of complex sectors or types of operations towards PA-aligned pathways.

- 2.18 **Practical and evidence-based assessments will promote learning.** In some instances, application of the PAIA can be complex, particularly given the fact that multiple pathways exist for long-term carbon neutrality and climate-resilient development (see ¶2.13). Even when countries have an LTS, assessing consistency at an individual project level may not lead to a clear-cut PA alignment determination. Therefore, when required, a specific assessment of PA alignment must be approached in a manner feasible for project teams. Application of the PAIA should promote the uptake of data and findings relevant to a specific context, consistent with best available science on how to meet the goals of the PA. Limited information will not prevent the application of the PAIA; at the same time, application of the PAIA should balance the materiality of risks and transaction costs for project preparation. The results from applying PAIA will be systematized in ways that inform future sector dialogues with the countries and when applicable, programming considerations, thus promoting learning cycles that further support countries' transition to long-term carbon neutrality and climate resilience.
- 2.19 **Leverages existing tools, expertise, and procedures at IDB Group for an integrated approach to climate risks and opportunities.** Several aspects of aligning to the PA intersect with environmental, social, and sustainability policies and governance, for example: with the application of the ESPF and the IDB Invest's Sustainability Policy and their Exclusion Lists, with mainstreaming and upstreaming of climate change, and with the promotion of climate finance (CF) and green finance (GF). The PAIA seeks to avoid duplications and maximize synergies with existing workflows (see Figure 4).
- 2.20 **Measures focus on long-term transformation.** Ultimately, PA alignment seeks to strengthen projects by helping connect short-term needs with longer-term imperatives to meet the goals of the PA (OECD, 2019). The objective is to minimize the long-term cost of the transition, bearing in mind that short-sighted or incremental mitigation or adaptation activities may result counterproductive to temperature and climate resilience objectives (Lütkehermöller & Pauthier, 2021), and more expensive and/or resource intensive. This guiding principle is one of the main value-adds from the PA assessment of operations.

Figure 4. Integration of PAIA to existing climate-related workflows at the IDB Group



- 2.21 **Possible inconsistencies with the goals of the PA.** A specific assessment for PA alignment is reserved exclusively for projects that are not deemed universally aligned to the mitigation goals of the PA or that may be inconsistent with climate resilience measures

in the national context. As deemed necessary, the PAIA will guide project teams, in coordination with respective clients, to consider alternatives, adjustments, and/or risk-management strategies to achieve alignment with the PA during project design. To this end, the IDB Group will provide clients with technical assistance to address systemic barriers (“climate transition gaps”)³¹ to achieve alignment. In the case such alternatives, adjustments, and/or risk-management strategies are not subject to be developed/implemented,³² the results of the PA assessment will be included as part of the operation’s proposal to be submitted for the consideration of the respective IDB Group Boards of Executive Directors.³³

III. Conclusion: Enabling Conditions for Successful Implementation

3.1 Expected impact. The PAIA has been designed to promote learning and improve understanding of the most appropriate criteria to ensure IDB Group provides enabling support to clients in meeting countries’ climate commitments under the PA. This process will impact IDB Group operations by: (i) substantially increasing IDB Group focus on helping LAC countries and businesses manage their transition to long-term carbon neutrality and climate-resilient economies; (ii) enhancing the management of climate-related risks in IDB Group’s lending portfolio; and (iii) sustaining and possibly increasing access to concessional resources for sustainable development, as PA alignment of an MDB’s operations becomes an access criterion. To fully attain this potential, the application of PAIA in new operations requires an enabling environment to be created through the following agenda of strategic actions:

A. IDB Group: Institutionalization, Communications, and Capacity Building

3.2 Establishment of a target for PA Alignment. In 2023, the possibility of setting a target of operations aligned to the PA will be discussed, as part of the update to the CRF. In that context, this PAIA and initial lessons learned will be presented to the Boards of Executive Directors for information and discussion as needed.

3.3 Registration and monitoring. PAIA requires cost-effective, system-based solutions for managing information in ways that facilitate monitoring, searching, learning and dissemination. As an immediate action, updates to the existing climate change module in Convergence (IDB), Maestro (IDB Invest), and Salesforce (IDB Lab) will be needed to record that the PAIA has been applied.

³¹ A term specific to the application of this PAIA, refers to barriers for full PA alignment such as infrastructure gaps, technology lags, policy and regulatory hurdles, or any other obstacle that make it unviable to deploy existing low-carbon or climate-resilient alternatives in a given local context. These will be systematically gathered to inform upstream policy dialogue to further advance the climate transition in such a context.

³² In this case, in accordance with the MDB Joint Methodological Approach, the operation is assessed as not aligned with the PA. A project’s non-alignment to the PA does not necessarily entail a country-level deviation from the country’s commitments under the PA. The PAIA does not provide an assessment of a country’s level of ambition, strategies, or priorities identified in its NDC or LTS.

³³ For IDB Invest, and as outlined in IDB Invest’s implementation approach, in the event a transaction is classified as not aligned and the classification conflicts with other financial and non-financial development priorities of IDB Invest, the Team Leader (INO) may bring the strategic element of the transaction to the Operations Committee (OC).

- 3.4 **Strategic Communications and Partnerships.** Awareness raising and dissemination of the concept of PA Alignment, what it means for doing business with the IDB Group,³⁴ should reach all operational staff by 2023, particularly those that engage directly with partners and clients. Collaboration with the Knowledge, Communications, and Innovation (KIC) sector is underway to develop a series of trainings for all types of audiences. Further outreach with Executing Agencies, Financial Institutions, Corporate Clients, and other partner organizations must continue throughout 2023 to disseminate IDB Group's approach to PA alignment. This will entail regional events and informational videos/interviews that will be made available in social media platforms. Partnerships with research centers on sectors where emissions are hard to abate (livestock, aviation, etc.) will also be encouraged to further advance the PA alignment agenda.
- 3.5 **Training program.** An ambitious agenda of strategic and technical training regarding the integrated approach to PA alignment, climate finance and green finance, has been designed by the KIC sector involving:
- a. Essential concepts of PA alignment, and its relationship to climate and green finance, for a general audience.
 - b. Strategic knowledge for decision-makers (e.g., country representatives and how to include PA alignment in the dialogue with governments and businesses).
 - c. Operational training for project teams, investment officers, clients, and Executing Agencies regarding the application of the PAIA.
 - d. Technical training for climate change and sector specialists who advise strategic selectivity and operational design.
- 3.6 **Additional needs for capacity building, analytical tools, and knowledge products.** The application of the Joint MDB Framework for PA alignment on past operations for the baseline assessment (Box 1), and additional analyses have made it possible to identify other required resources to successfully implement this approach:
- a. A multi-year training program that helps consolidate the PA alignment framework across technical teams in charge of project preparation.
 - b. A required online course on identifying and managing climate risks and opportunities in operations. This will have an emphasis on the importance of upstream dialogue to create demand for development alternatives that are consistent with the long-term carbon neutral and climate-resilient trajectories of the PA, and that underscore the benefits for development and competitiveness of the region of orderly and timely transitions.
 - c. Dedicated training programs with financial institutions; consider a platform or facility to provide permanent support for strengthening climate governance.³⁵

³⁴ A dedicated communications strategy may be needed for operations where the specific assessment of PA Alignment indicates that components or activities are difficult to align to PA mitigation or adaptation pathways.

³⁵ Preliminary estimates indicate an integral support for PA alignment in the area of financial institutions in the public and private sectors will require approximately US\$10 M across the next three years.

- d. Additional sector-specific technical guidance on operations related to high-emitting industries, buildings, and digital technologies.
- e. A toolkit of resources and agreed detailed methods for PA alignment assessments (e.g., subsector-specific carbon lock-in analyses; updates to economic, cost-benefit, and financial analyses to account for climate variables; incorporation of climate risks in the assessment of macroeconomic policy frameworks, etc.).
- f. Digital tools for emissions accounting and rapid assessment of PA alignment.
- g. Agile PA alignment tools and sector guidance applicable to IDB Lab's mandate, that is responsive to the needs of its unique clients and stakeholders.
- h. Tools and methodological approaches to reinforce environmental standards related to the protection of high carbon stocks, particularly through value chains.

3.7 **Continue a dialogue on key methodological issues that remain unclear.** Through baseline assessments and pilot applications of the Joint MDB Framework for Paris Alignment, technical teams have identified aspects of PA alignment that require further clarification through continued practice and learning. These include issues such as: (i) setting criteria to consistently define the extent of project boundaries for the PA alignment assessment; (ii) setting SMART indicators for climate adaptation, low-carbon and climate resilient development; (iii) operationalizing the concept of maladaptation; (iv) establishing criteria to quickly assess and determine instances where the risk of stranded assets is considered material; (v) defining the extent or scope with which policy reforms have a bearing on long-term emissions and climate adaptation trajectories; and (vi) assessing project exposure to transition risks, distinguishing public and private sectors.

B. IDB Enabling Conditions

3.8 **Clear coordination for climate-related risk management roles.** Specific Standard Operating Procedures (SOPs) detailing the interaction of work between ESG and CCS for PA alignment documentation, to ensure coordination on the application of ESPF Standards 1, 3, and 4 and overlapping risks related to PA alignment. Also, collaboration with RMG/ESR to create general literacy on the identification and management of climate transition risks, as applicable to public sector operations.

3.9 **Integrated update for climate-related roles and responsibilities in project preparation.** Based on lessons learned from Climate Finance implementation and the initial application of this PAIA, the Procedures for Processing Sovereign-Guaranteed Operations (PR-200 Annex I Summary Chart of Processing) should be updated to reflect climate and sustainability-related tasks during project preparation. These now will span across the application of MDB guidance for Climate Finance and PA Alignment, as well as the identification of Green Finance according to IDB Group's own methodology.

3.10 **Budgeting support.** For adequate implementation, the application of PAIA requires a consistent flow of additional resources in two main modalities: (i) technical assistance; and (ii) human resources.

- a. **Technical assistance:** To cover the incremental cost of low-carbon and climate-resilient alternatives in operations that present "climate transition gaps"; to perform additional technical and/or economic studies for operations (e.g., analysis of alternatives given their carbon lock-in risk, traceability of value chains,

quantification of transition risk scenarios and stranded assets in financial sensitivity analyses, etc.). But also, regionally adjusted sector-specific analyses to further characterize decarbonization pathways (specific criterion 3 of the mitigation methodology) with details of the feasibility of technical shifts within LAC and its subregions. There is also a need for analyses that help catalyze public and private synergies for PA alignment in key sectors.

- b. **Human resources:** These include both permanent personnel which are necessary to ensure consistency in the approach with continuity in its application; and rotational personnel to assist in the technical landing of concessional resources, training, and logistics associated to implementation. Human resources are needed in-terrain, to strengthen technical capacities within the IDB and executing agencies regarding PA alignment, to guide country analysis and strategy, and to deploy additional assistance for operations on-demand. They are also needed in headquarters, to build internal capacity in monitoring the portfolio, to strengthen capacities regarding the application of the ESPF, to provide quality assurance in the application and reporting of the assessment framework, and to engage with relevant stakeholders as the MDB approach evolves.

- 3.11 The resources for technical assistance will be predominantly sought from sources of non-reimbursable resources administered by the IDB. Human and financial resources required for implementation of the PAIA were considered in the 2023 IDB Group budget. Resource availability beyond 2023 will be discussed in future budget exercises.

C. IDB Invest Enabling Conditions

- 3.12 **Strategic alignment with IDB Invest 2.0.** The PAIA must be optimally aligned to IDB Invest business plan. The future portfolio should be guided by a programmatic focus that includes synergies with the public arm of the IDB Group, strategic selectivity, and development impact.

- 3.13 **Budgeting support.** A consistent flow of additional resources is necessary for adequate implementation of PAIA in IDB Invest. The additional resources are required for technical assistance and human resources:

- a. **Technical assistance:** On a case-by-case basis, IDB Invest will support clients onto PA aligned pathways through technical assistance on adaptation and mitigation. As an enabling condition, additional resources will be required for such technical assistance commensurate with pipeline volume.
- b. **Human and financial resources:** Where a detailed analysis is required to assess alignment with BB1 and/or BB2, is it anticipated IDB Invest can conduct most detailed analyses in-house, contingent on the availability of additional in-house capacity for the technical teams involved in the BB1 and BB2 assessment (DSP/ADV, DSP/SEG). In more complex cases, external consultancy will be required, with an estimated cost per analysis of between US\$80,000-100,000 for external detailed BB1 assessments, and US\$60,000-200,000 for external detailed BB2 assessments.

- 3.14 **Continuously improve IDB Group training programs.** In collaboration with the KIC sector, project teams and country offices will be provided with strategic and technical training with a specific focus on PA alignment in the private sector.

D. IDB Lab Enabling Conditions

- 3.15 **Strategic alignment with IDB Lab's Business Plan 2022-2023.** Ensure PAIA is optimally aligned to IDB Lab's Business Plan and ongoing refinement to IDB Lab's operational model which places growing relevance on financial returns. PA alignment of the future portfolio will consider IDB Lab's unique mandate, clients, financial and non-financial product offerings, and transaction cost associated with smaller ticket size.
- 3.16 **Integrated application of PA alignment frameworks.** IDB Lab will work closely with key organizational units across the Bank, such as Environmental and Social Safeguards Unit (ESG), the Office of Strategic Planning and Development Effectiveness (SPD), among others, to develop and institute mechanisms that will enable early screening, alignment checks and reporting on PA alignment –including development of PA alignment knowledge briefs to guide project teams in priority sectors.
- 3.17 **Update iDELTA.** Explore opportunities to acknowledge and quantify the impact of PA alignment in the iDELTA score of projects, and to track this over time.
- 3.18 **Digital PA alignment toolkit for innovators.** In collaboration with the Bank, develop a digital toolkit to support both design teams and clients apply PA alignment frameworks in the context of innovation for inclusion.
- 3.19 **Continuously improve IDB Group training programs.** In collaboration with the KIC sector, project teams and country offices will be provided with strategic and technical training with a specific focus on PA alignment in the context of IDB Lab's unique mandate, focus on innovation for inclusion and unique private sector clients.

E. Next steps

- 3.20 As a technical tool, the PAIA will provide valuable information when preparing new operations. The approved PAIA will be distributed to the Boards of Executive Directors for information. In parallel, documents detailing the additional guidance requirements presented above in [Table 1](#) will be approved by Management to be used by project teams.

Appendix 1: Activities Considered Universally Aligned to Mitigation Goals of the PA

The following draft list reproduces the Appendix of the Joint MDB Assessment Framework for Paris Alignment for Direct Investment Operations.³⁶

Operation types included on this list will have to go through the specific criteria assessment if they fall under any of the following:

- i. Operations whose economic feasibility depends on external fossil fuel exploitation, processing, and transport activities (e.g., a railway line that will have a significant income from the transport of coal from a coal mine).
- ii. Operations whose economic feasibility depends on existing fossil fuel subsidies (e.g., a fishing fleet that would be unfeasible in the absence of subsidies to diesel fuel).
- iii. Operations that rely significantly on the direct utilization of fossil fuels (e.g., a pharmaceutical production plant that makes use of diesel pumps).

Sector	Eligible operation type	Conditions and guidance
Energy	Generation of renewable energy (e.g., from wind, solar, wave power, etc.) with negligible lifecycle GHG emissions.	Includes generation of heat or cooling
	Rehabilitation and desilting of existing hydropower plants, including maintenance of the catchment area (for example, a forest management plan)	Rehabilitation includes work on the water holding capacity of the dam and work on pipes/turbines to increase productivity and bring additional grid stabilization benefits, and for pumped storage
	District heating or cooling systems with negligible lifecycle GHG emissions	Using significant renewable energy or waste heat or cogenerated heat OR Including: a) Modification to lower temperature delta b) Advanced pilot systems (control and energy management, etc.)
	Electricity transmission and distribution, including energy access, energy storage, and demand-side management	
	Cleaner cooking technologies	Cleaner cooking technologies substitute the use of traditional solid biomass fuels in open fires; they include sustainable biomass or electric cookstoves

³⁶ The list is subject to updates by MDBs in future revisions of the Joint MDB Methodological Approach for Assessment of Paris Alignment.

Sector	Eligible operation type	Conditions and guidance
Manufacturing	Non-energy-intensive industry (excludes chemicals, iron and steel, cement, pulp and paper, and aluminium)	Consider the nature of the product produced (carbon content, lifetime, ability to be reused/recycled).
	Manufacture of electric vehicles; non-motorized vehicles, electric locomotives; non-motorized rolling stock	
	Manufacture of components for renewable energy or energy efficiency	
Agriculture, forestry, land use and fisheries	Afforestation, reforestation, sustainable forest management, forest conservation, soil health improvement	With the exception of operations that expand or promote expansion into areas of high carbon stocks or high biodiversity areas
	Climate-smart agriculture	With the exception of operations that expand and promote expansion into areas of high carbon stocks or high biodiversity areas and taking into account (international) transport
	Conservation of natural habitats and ecosystems	With the exception of operations that expand or promote expansion into areas of high carbon stocks or high biodiversity areas
	Sustainable fishing and aquaculture	
	Flood management and protection, coastal protection, urban drainage	
Waste	Separate waste collection (in preparation for reuse and recycling), composting and anaerobic digestion of biowaste, material recovery, and landfill gas recovery from closed landfills	
Water supply and wastewater	Water supply systems (e.g., expansion, rehabilitation); water quality improvement; water efficiency (e.g., non-revenue water reduction, efficient process in industries); drought management; water management at watershed level	Desalination plants need to go through specific assessment
	Gravity-based or renewable energy-powered irrigation systems	
	Wastewater treatment (domestic or industrial), including treatment and collection of sewage, sludge treatment (e.g., digestion, dewatering, drying, storage), wastewater reuse technology, resource recovery technologies (e.g., biogas into biofuel, phosphorus recovery, sludge as agriculture input, sludge as co-combustion material)	
Transport	Electric and non-motorized urban mobility	
	Roads with low traffic volumes providing access to communities which currently do not have all-weather access (for example, connecting farmers to markets or providing access to a rural school, hospital, or better social benefits)	Except if there is any risk of contributing to deforestation
	Electric passenger or freight transport	
	Short sea shipping of passengers and freight ships	
	Inland waterways passenger and freight transport vessels	

Sector	Eligible operation type	Conditions and guidance
	Port infrastructure (maritime and inland waterways)	
	Rail infrastructure	
	Road upgrading, rehabilitation, reconstruction, and maintenance without capacity expansion	
Buildings and public Installations	Buildings (education, healthcare, housing, offices, retail, etc.)	Needs to meet green building certification criteria as established by each individual MDB ³⁷
	LED street lighting	
	Parks and open public spaces	Excluding energy-consuming installations ³⁸
Information and communications technology (ICT) and digital technologies	Information and communication, excluding data centers	
Research, development and innovation	Professional, scientific, research and development (R&D), and technical activities	
Services	Public administration and compulsory social security	
	Education (excluding infrastructure/buildings)	
	Human health and social work activities (excluding infrastructure/buildings)	
	Social protection, cash transfer schemes	
	Arts, entertainment and recreation (excluding infrastructure/buildings)	
Cross-sectoral activities	Conversion to electricity of applications that currently use fossil fuels	

Source: (MDB Group, 2021)

Note: operations related to urban development and tourism will be assessed using this list as appropriate, assessing components according to categories such as “buildings and public installations”, “land use”, “services” “waste”, “water supply and wastewater” and “transport”.

³⁷ MDBs are working on the approach to assess the Paris alignment of buildings and the role of certification schemes. This approach can also take into account the impact of materials on the alignment of buildings with the low-carbon pathways envisioned by the Paris Agreement.

³⁸ Energy-consuming installations are those beyond lighting and routine maintenance such as watering. Examples are major built-up area (i.e., buildings) or energy-intensive installations (e.g., fountains or playground and recreational equipment that need a non-renewable power source).

Appendix 2: Activities Considered Universally Not Aligned to Mitigation Goals of the PA

At this time, the MDBs consider four activity types to be universally not aligned with the Paris goals:

- Mining of thermal coal;
- Electricity generation from coal;
- Extraction of peat; and
- Electricity generation from peat.

Note that the fact that being omitted from this list does not mean that an operation type is endorsed by or will be financed by the MDBs.

GLOSSARY

Concept	Definition
Activities aligned with the mitigation goals of the PA	Activities that either qualify as universally aligned, or that validate their alignment to the PA mitigation goals through a specific assessment (BB1).
Activities aligned with the adaptation goals of the PA	Activities that validate their alignment to the PA adaptation goals through the three-step MDB framework for climate adaptation and resilience (BB2).
Activities universally aligned to the mitigation goals of the PA	Activities considered by the MDBs to be aligned to the mitigation goals of the PA across countries and under all circumstances. Included in Annex 1 of the Joint MDB Framework for Assessing PA Alignment of Direct Investments. These include climate-positive activities (e.g., renewable energies that reduce CO2 emissions) and climate-neutral activities (e.g., public administration services).
Activities universally not aligned with the PA	Activities considered by the MDBs to be not aligned with the mitigation goals of the PA across countries and under all circumstances. At the time of writing: extraction and/or electricity generation from coal and peat.
Carbon lock-in	According to the Joint MDB Assessment Framework for PA alignment, technical, economic, or institutional factors associated with an investment result in that asset continuing to operate in an emissions-intensive way, even when there are feasible and economically preferable lower carbon options that could replace it.
Climate-related risks	Risks related to the transition to a lower-carbon economy (such as extensive policy, legal, technology, and market changes to address mitigation and adaptation requirements related to climate change) and risks related to the physical impacts of climate change on the project (such as such direct damage to assets due to changes in water availability, sourcing, and quality, significant temperature changes affecting organizations' assets, infrastructures, operations, supply chain, transport needs, and employee safety).
Climate transition gaps	A term specific to the application of this PAIA, refers to infrastructure gaps, technology lags, policy and regulatory barriers, or any other obstacle that make it unviable to deploy existing low-carbon or climate-resilient alternatives in a given local context. These will be systematically gathered to inform upstream policy dialogue to further advance the climate transition in such a context.
Cost-effectiveness	Economic rationale of a measure, determined according to capital and operational costs, financial benefits, and environmental and social externalities of the measure, considered over the life of the operation (IDB, 2020).
Financial feasibility	Calculation based on financial considerations, including relative magnitude of the incremental cost of adopting measures and actions compared to the project's investment, operating, and maintenance costs (IDB, 2020).
High Carbon Stocks (HCS)	Forests identified through the HCS Approach as forested areas to be prioritized for protection from conversion, through an integrated land use planning perspective. The HCS approach distinguishes above-ground biomass in trees

Concept	Definition
	greater than or equal to 5cm DBH (diameter at breast height) as a proxy of viable forest areas with dense vegetation (relatively high levels of perennial woody biomass), in opposition to degraded areas that have lower carbon and biodiversity values. It is meant to be integrated with other methods for land conservation (HCS Approach Steering Group, 2015).
Indirect impact	An impact caused by the project generally, but not always, later in time or farther removed than a direct impact but is still reasonably foreseeable and may include effects related to changes in the pattern of land use, population density, related effects on air and water and other natural systems, inc. ecosystems (IDB, 2020).
Just Transition	Support for low greenhouse gas emissions and climate resilient strategies through measures where associated costs and benefits are fairly distributed (MDB Working Group, 2020). Just transition measures refer to policy interventions that aim to shift the economic structure to a low-carbon, socially and environmentally friendly one and, when doing so, maximize the benefits, minimize and compensate costs, and give voice to all stakeholders affected by climate policy (Saget, Vogt-Schilb, & Luu, 2020).
Long Term Strategies	LTSs are understood as overall national, subnational, or supranational strategies for achieving low-emission long-term (often focused on mid-century) development, considering broader sustainability, socioeconomic, and climate change adaptation goals. MDBs have agreed on a set of key Principles for Long-Term Strategy Support , which include ambition, just transition, clear steps with near and medium-term milestones, and country ownership.
Maladaptation	Actions that increase current or future climate vulnerabilities within the boundaries of an operation, shift vulnerabilities from within the boundaries of an operation to an external/surrounding system (causing adverse effects on social, environmental, economic, or physical aspects of the system), or undermine sustainable development. Maladaptation occurs when an action undermines the coping capacities of existing systems, diminishes the capabilities of future generations to respond to climate vulnerabilities, or places a disproportionate burden for climate action on present-day or future external actors.
Multiple Works Operations	Operations involving a group of similar works and typically share the following characteristics: (i) they are physically similar but independent of each other; (ii) feasibility does not depend on the execution of any particular number of the works projects; and (iii) individual size does not warrant direct IDB lending.
Operations with financial intermediaries	The financing structure involves the provision of funds through financial institutions or through delivery mechanisms involving intermediation whereby the financial institution undertakes the task of subproject appraisal and monitoring.
Stranded assets	Those that have suffered from unanticipated or premature write-downs, devaluations, or conversion to liabilities due to climate change impacts. These could entail an asset losing value, solvency risks from reduction in credit rating, liquidity risks, lower than expected return on investment (Caldecott, 2013).

Concept	Definition
Scope 3 / value chain emissions	These refer to activities from assets not owned or controlled by the client, but that indirectly impact its value chain.
Technical feasibility	As established in the ESPF, based on whether the proposed measures and actions can be implemented with commercially available skills, equipment, and materials, taking into consideration prevailing local factors such as climate, geography, infrastructure, security, governance, capacity, operational reliability.
Transition finance	Economic activities that are emissions-intensive, but that do not currently have a viable low-GHG substitute (technologically, economically or both) and are important for socio-economic development.
Transition risks	Those that emerge from transitioning to a lower-GHG economy, which may entail extensive policy, legal, technology, and market changes to address mitigation and adaptation requirements related to climate change. Depending on the nature, speed, and focus of these changes, transition risks may pose varying levels of financial and reputational risk to organizations (TCFD, 2017). These span aspects such as: increased operating, capital, and insurance costs, as well as asset depreciation; increase in operating and/or litigation costs; forced capital depreciation; value loss of existing assets; reduced demand for products and services; costs of developing and procuring new technology; reduced demand; costs from unexpected market changes in supply chains; reduced revenue due to demand, production, capital availability and employee attractiveness, etc.

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