



Program Information Document (PID)

Concept Stage | Date Prepared/Updated: 11-May-2023 | Report No: PIDC35434



BASIC INFORMATION

A. Basic Project Data

Country Ecuador	Project ID P180319	Project Name Ecuador Third Green and Resilient Recovery DPF (EGARR-DPF3) (P180319)	Parent Project ID (if any) P178636
Region LATIN AMERICA AND CARIBBEAN	Estimated Board Date Jul 31, 2023	Practice Area (Lead) Macroeconomics, Trade and Investment	Financing Instrument Development Policy Financing
Borrower(s) Republic of Ecuador	Implementing Agency Ministry of Economy and Finance		

Proposed Development Objective(s)

The Program's Development Objective (PDO) is to assist the government of Ecuador in its agenda to tackle selected structural challenges to foster inclusive, resilient, and low-carbon development.

Financing (in US\$, Millions)

SUMMARY

Total Financing	500.00
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DETAILS

Total World Bank Group Financing	500.00
World Bank Lending	500.00

Decision

The review did authorize the preparation to continue



B. Introduction and Context

Country Context

1. **The proposed Third Green and Resilient Recovery Development Policy Financing (DPF), for US\$500 million, is the final operation in a programmatic series of three.** The series seeks to assist the Government of Ecuador (GoE) in tackling selected structural challenges to foster inclusive, resilient, and low-carbon development. The first operation, for US\$700 million,¹ was approved by the World Bank's (WB) Board of Executive Directors in February 2022, and the second operation, for US\$500 million, was approved in December 2022. This programmatic series is fully aligned with the National Development Plan 2021-2025 (*Plan de Creación de Oportunidades 2021-2025*, NDP), which focuses on the country's medium and long-term development goals to reduce poverty and increase shared prosperity. It is also aligned with the Country Partnership Framework (CPF) FY2019-2023, and the World Bank Group (WBG) Roadmap for Climate Action in Latin America and the Caribbean² as it focuses on transitioning to a green, inclusive, low-carbon and resilient development pathway.

2. **Despite substantial progress in rebalancing the economy, Ecuador still needs to address structural challenges to consolidate fiscal sustainability, achieve inclusive growth, and protect vulnerable people by increasing inclusion and social resilience.** After rebounding 4.2 percent after the pandemic-led 2020 recession, Gross Domestic Product (GDP) grew to 2.9 percent in 2022 as some sectors continued recovering from the pandemic and others benefited from high commodity prices, offsetting the adverse effects of a prolonged protest and sporadic disruption in oil production due to damages to the pipelines caused by demonstration and the regressive erosion of Coca River and its tributaries. The fiscal deficit was reduced from 1.7 percent of GDP in 2021 to near balance in 2022 due to recovering economic activity, improving oil prices, 2021 tax reform, sustained public expenditure rationalization, and friendly debt renegotiations with China. As a result of this fiscal consolidation and economic recovery, public debt has decreased from a peak of 62.3 percent of GDP in 2021 to 58.1 percent in 2022, and international reserves rose from a low of 2.4 percent in 2017 to 7.3 percent in 2022, restoring confidence in dollarization and macroeconomic stability.

3. **Ecuador's high exposure to climate-related disasters calls for enhanced efforts to foster green and resilient growth.** Ecuador is among the 10 countries with the highest natural disaster risk, particularly exposed to earthquakes, recurrent floods, and intensifying droughts. Vulnerability to phenomena like the El Niño Southern Oscillation (ENSO) and related disasters such as floods and landslides is exacerbated by the fact that 96 percent of the urban population lives in the coastal and mountainous regions. Ecuadorian firms lose US\$1 billion annually due to infrastructure disruptions, mainly transport and power.³ In March 2023, the country was hit by a 6.8 earthquake that killed at least 14 people and, in conjunction with a heavy rain season, caused damage for about US\$200 million. Ecuador has much to gain from global efforts to combat climate change⁴ and is committed to decoupling growth from greenhouse gas (GHG) emissions.

¹ The Ecuador Green and Resilient Recovery (EGARR, P176983) DPF was approved by the WB's Executive Board on February 1st, 2022 and became effective on February 24th, 2022.

² World Bank Group. 2021. [Climate Change Action Plan 2021-2025: Supporting Green, Resilient and Inclusive Development](#). Washington D.C.

³ IADB. 2021. Políticas climáticas en América Latina y el Caribe: Casos exitosos y desafíos en la lucha contra el cambio climático.

⁴ Countries can prioritize sustainable development when well-designed climate change mitigation, and adaptation and resilience measures generate enormous economic, social, and environmental benefits. According to a recent ILO/IDB study, a decarbonization-focused recovery could generate 15 million jobs in Latin America. Studies have identified that infrastructure investment paths can be compatible with full decarbonization and they do not need to cost more than more polluting alternatives (Rozenberg, Fay. 2019. *Beyond the Gap: How Countries Can Afford the Infrastructure They Need while Protecting the Planet*). With the right policies, investments of 4.5 percent of GDP would enable low- and middle- income countries to achieve the infrastructure-related sustainable development goals and stay on track to limit climate change to 2°C. In Chile the Ministry of Finance, with support from the WB, led a study (Green Growth Opportunities for the decarbonization goal for Chile, published 2020), concluding that implementing a



Relationship to CPF

4. **The DPF series play a central role in the WBG's engagement with Ecuador and is fully aligned with the WBG's FY19-FY23 CPF (report no. 135374-EC, discussed by the Board of Executive Directors in June 2019).** The CPF focuses on achieving the WBG's twin goals—ending extreme poverty and boosting shared prosperity—through three interdependent areas: (i) Supporting Fundamentals for Inclusive Growth, (ii) Building Human Capital and Protecting the Poor, and (iii) Enhancing Institutional and Environmental Sustainability. Pillar 1 of the proposed DPF series supports CPF objectives under results areas (i), (ii), and (iii), and Pillar 2 supports CPF objectives under results area (iii).

5. **The third DPF will complement the Harnessing the Potential of Forests for Sustainable Development in Ecuador (P178622), which aims to implement sustainable forest management policies and biodiversity value chains in selected landscapes.** The DPF supports regulatory reforms related to sustainable forest management and will inform the investment lending operation under preparation. In turn, the IPF will contribute to building the technical and financial capacities to support the implementation of sustainable forest management policies and sustainable forestry value chains.

C. Proposed Development Objective(s)

6. The Program's Development Objective (PDO) is to assist the GoE in its agenda to tackle selected structural challenges to foster inclusive, resilient, and low-carbon development.

Key Results

7. The expected results of this operation include Ecuador's macro-fiscal policies and practices aligning with its climate goals and adopting a budgeting approach that prioritizes climate-responsive investments and moves from greening projects to greening the economy. These structural changes are expected to foster growth potential and protect the vulnerable population. The structural reforms can bolster private investment as they reduce the cost of imported capital goods such as machinery and mechanical appliances, increase the participation of the private sector in the provision of non-conventional renewable energy (NCRE), and reduce GHG emissions generated from gas flaring and by improving sustainable forest management.

D. Concept Description

8. **Pillar 1 of the third DPF operation supports critical structural reforms to foster green growth, inclusion, and climate resilience.** It strengthens the fiscal framework by enhancing the institutional setup to address climate-related challenges, including climate budget planning and disaster risk fiscal impacts. These measures are relevant to support the implementation and monitoring of economy-wide climate programs and to provide a systematic way of assessing fiscal contingency risks to PPP projects. They also support reforms to foster social inclusion and resilience by including measures to integrate Venezuelan migrants, including children and adolescents separated from their families and those traveling alone, and protect victims of human trafficking and natural disasters, including those associated with climate change. This last set of reforms is critical for the most vulnerable women as potential beneficiaries of social assistance programs and partially addresses the disproportionate burden women have suffered during the COVID-19 pandemic and other weather-

mitigation policy package, jointly proposed by the Ministries of Energy, Environment, and Agriculture, can have a positive impact on the economy, that could mean an additional growth of 4.4 percent of its GDP by 2050 and could translate into an additional US\$31 billion towards the country's economic development.



induced disasters.⁵

9. **Actions under Pillar 2 support the GoE's efforts to strengthen low-carbon development.** The measures are aligned with the WBG Roadmap for Climate Action in Latin America and the Caribbean as they seek to prioritize actions on the largest mitigation opportunities to help integrate climate and development in Ecuador. They aim to promote private capital mobilization and green growth. The key sectors contributing to GHG emissions in Ecuador are land-use change and forestry, accounting for 27 percent of emissions, energy with 25 percent, and transportation with 20 percent. Reforms under this pillar focus on mitigation measures with the potential for a green and resilient economic recovery by promoting private investment in NCRE energy, encouraging gas-flaring reduction and increased energy efficiency, transport decarbonization and safety, promoting sustainable forest management, and supporting the development of voluntary carbon-trading markets through the strengthening of compensation mechanism and emission registry to help mitigate GHG emissions.

10. **The proposed operation is aligned with the goals of the Paris Agreement, provides significant climate co-benefits, and is broadly aligned with the Green, Resilient, and Inclusive Development (GRID)⁶ framework, the Global Crises Response Framework (GCRF),⁷ and the WBG Roadmap for Climate Action in Latin America and the Caribbean.** All prior actions of the proposed DPF are aligned with the goals of the Paris Agreement as they are consistent with the country's NDC, they are not likely to cause a significant increase in GHG emissions or barriers to transition to low-GHG emissions, and their contributions to the PDO are not expected to be affected by climate hazards, but to increase the resilience of the Ecuadorian population. The reform program is aligned with three out of four GCRF pillars: (ii) Protecting people and preserving jobs; (iii) Strengthening resilience; and (iv) Strengthening policies, institutions, and investments for rebuilding better. On the adaptation to increased climate-related shocks, the proposed operation acknowledges GoE's efforts to increase its ability to confront climate impacts by reducing its fiscal risks by targeting fuel subsidies, a low-carbon growth initiative. This action complements previous efforts to reduce oil export revenues' dependency and advance Ecuador's NDC commitments on adaptation and mitigation efforts. Adaptation is reflected in the GoE effort to enhance the institutional setup to handle climate disaster risks and improve public services to take malnutrition while strengthening gender equality. On the mitigation side, the proposed operation includes actions to enhance the energy sector's decarbonization by promoting distributed non-conventional energy generation, reducing tariffs on lithium battery imports, setting decarbonization strategies in the energy sector, improving transport efficiency, fostering the development of voluntary carbon markets, and promoting sustainable forest management to reduce deforestation and increase conservation and restoration. Therefore, the operation addresses critical mitigation levers identified by the Intergovernmental Panel on Climate Change (IPCC) and in the NDC commitments of Ecuador to implement its goals under the Paris Agreement.

E. Poverty and Social Impacts, and Environmental, Forests, and Other Natural Resource Aspects

Poverty and Social Impacts

11. **Prior Actions supported under Pillar 1 are expected to have minor impacts on poverty and inequality in the**

⁵ Around one-fifth of individuals have lost their job since the onset of the pandemic in Ecuador, of which 60 percent are women. Women are more likely to be in more precarious employment pre- and post-COVID-19 as informality rates were two percentage points higher for women than for men in 2019 (i.e., 47.9 and 45.9 percent respectively), and the gap widened to four percentage points in 2020 (i.e., 53.4 vs. 49.5 percent respectively). Women were more likely than men to withdraw from the labor market due to the need to take care of children and the elderly at home. Women work 20 hours more per week than men in unpaid work such as food preparation, cleaning, dwelling, laundry, and childcare.

⁶ World Bank. 2021. [From COVID-19 Crisis Response to Resilient Recovery - Saving Lives and Livelihoods while Supporting Green, Resilient and Inclusive Development \(GRID\)](#).

⁷ World Bank. 2022. [Navigating Multiple Crises, staying the course on Long-Term Development. The World Bank Group's Response to the Crises affecting Developing Countries](#).



short-term but positive effects on households' welfare in the medium to long run. The removal of the fuel subsidy for large shrimp farms in PA1 is not expected to significantly impact poverty due to the remaining quota for small and artisanal shrimp farm production and small businesses in the sector. Moreover, the share of the subsidy as the total cost for firms is small and will unlikely affect job security. Setting the institutional framework for future issuance of green bonds in PA2 is expected to bring minor indirect positive welfare impacts in the long run, conditional on the use of resources; special consideration of the constitution of risk across different scales and social groups might be important to prevent adverse impacts on inequality. Quantifying contingent liabilities caused by climate and climate-related disasters for PPP projects on PA3 could positively affect welfare by procuring more resilient infrastructure (e.g., energy, transport, and water sanitation), thus protecting the most vulnerable users from the negative impacts of natural disasters. The implementation of a partly conditional cash transfer (Bono 1000 días) for poor pregnant women and children up to 2 years old is expected to have positive welfare impacts in the medium to long run, considering that investments in early childhood have proven crucial to improve health, economic and social outputs at the individual and society levels, and considering that a conditional component will promote access to important complementary services (early childhood development, health controls) to improve children's nutrition in the first 1000 days –a critical period of physical and cognitive development. Implementing an extraordinary regularization process for Venezuelans and refugees and the decree for phases 2 and 3 on PA4 are expected to have small positive welfare impacts in the medium to long term. Regularization is necessary to improve people's employability while lowering pressure on more vulnerable low-skilled workers in host communities and enabling access to public services and social protection. However, complementary actions may be needed to materialize the opportunities that come with migration. In addition, the implementation of the gender-inclusive strategy in the power sector is expected to have small but positive impacts on equity, considering that these guidelines aim at improving the working conditions of women, training for women, and positive discrimination in hiring procedures and procurement processes in the electricity sector, where women represent only 18.2 percent of workers and earn 13 percent less than their male counterparts (Enemdu Annual, 2022).

12. Prior Actions supported under Pillar 2 aimed to strengthen low-carbon development are not expected to impact the well-being of poor households in the short term; still, positive effects are expected in the medium and long term. Regulations to distribute renewable energy among non-regulated customers and by reducing tariffs on lithium batteries at the residential and commercial level and investment in PA5 are expected to positively affect households' welfare by increasing private investment in clean energy projects, which could lead to lower generation costs, affordable energy access in remote areas, and green job creation. Creating a decarbonization committee by PetroEcuador, implementing financing mechanisms to support the energy transition to cleaner and more sustainable energy sources in oil companies, and requiring power distribution companies to present their energy efficiency plans in PA 6 could positively impact well-being by fostering energy efficiency investment in the oil sector, creating new jobs in the energy sector, and reducing negative externalities associated with fossil fuel use, such as adverse health impacts, particularly of poor households living nearby oil fields. The secondary regulation to the Organic Law on Land Transportation, Transit, and Road Safety in PA7 would not impact poverty or inequality reduction immediately, yet positive effects are expected in the long term by potentially reducing air pollution in cities, improving the quality of public transportation, and promoting a transition to lower-carbon vehicles. Neutralization mechanisms under *Programa Ecuador Carbono Cero* (PECC) in PA8 are not expected to affect welfare in the short run. In the medium to long run, impacts will likely depend on project implementation and its interaction with other environmental policies, but some positive effects could be expected from the health and environmental co-benefits of reduced pollution. In addition, improving sustainable forest management could create opportunities for poor households in rural areas, such as indigenous groups whose subsistence and income depend on forest products. Thus, preparing, approving, registering, and updating integrated forest management plans in PA9 and regulation on traceability of timber and non-timber export and imports; and homologation of forest professionals and advisors in PA10 could positively impact the welfare of rural populations by creating better economic opportunities aligned with sustainable forest management and increasing the value of wood and non-wood forest products, and being an



inclusion mechanism into the formal economy of poor communities that depend on forestry products.

Environmental, Forests, and Other Natural Resource Aspects

13. **The measures supported under Pillar 1 are expected to positively affect the environment, forests, or other natural resources.** Eliminating the diesel subsidy for large shrimp farms (PA1) is expected to incentivize more efficient fuel use, reducing GHG emissions. Likewise, setting up the institutional and governance framework for green bond issuance (PA2) and enhancing the Government's capacity to quantify contingent liabilities caused by climate-related disaster in PPP projects (PA3) are expected to have a positive effect on the environment as it will allow the authorities to better manage risk and opportunities arising from climate change and global decarbonization agenda. Actions proposed under PA4 related to fostering inclusion and social resilience to support the most vulnerable are expected to have neutral effects.

14. **Policy measures supported by Pillar 2 related to strengthening low-carbon development are expected to have positive effects on the environment, forests, or other natural resources.** Measures to foster promote distributed renewable generation and the reduction of tariff to lithium batteries (PA5) are likely to underpin the transition to greener energy source. In the same vein, the government effort to promote decarbonization in PetroEcuador, require energy efficiency plans in the power distribution companies, and set up mechanism to finance capex on energy efficiency measures (PA6) are likely to foster the government decarbonization effort. PA7 aims to develop regulations promoting greener transportation and is also expected to have positive effects on the environment by lowering CO2 emissions in the urban transport sector. Similarly, PA8, which relates to establishing a neutralization mechanism for public and private entities that reduce GHG emissions and promote resilience in non-forest areas, is expected to result in positive effects for the environment by aiming to achieve carbon neutrality in the productive and service sectors. PA9 and 10, which foster sustainable forestry management by promoting deforestation-free integrated forest management plans and enacting regulations on the traceability of timber and non-timber exports and imports, and homologating forest professionals and advisors, are expected to result in better forest conservation while promoting sustainable management practices.

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APPROVAL

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