

# Financing the Future

## Sustainable Finance

### Latin America 2023 Outlook

INFORMATION, INSIGHTS, AND IDEAS

JANUARY 2023

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Scotiabank is a leading bank in the Americas and the only Canadian bank with operations in Canada, the U.S., the Pacific Alliance countries and Brazil. Guided by our purpose: “for every future,” we help our customers, their families and their communities achieve success through a broad range of advice, products and services, including personal and commercial banking, wealth management and private banking, corporate and investment banking, and capital markets. Scotiabank believes the Pacific Alliance region (Mexico, Peru, Chile and Colombia) and Brazil offers excellent opportunities for growth with pro-business policies, favourable demographics, good economic growth, low consumer indebtedness and stable banking systems.

#### LATIN AMERICA SUSTAINABLE FINANCE

Scotiabank’s Sustainable Finance team had a strong 2022 in Latin America amid volatile market conditions, with the team being recognized with three LatinFinance awards in 2022, including Sustainable Finance Bank of the Year, Infrastructure Financing of the Year, and Renewable Energy Financing of the Year.

## Executive Overview

### 2022 Trends and Year in Review

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- **Increased Innovation**
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### 2023 Sustainability Outlook

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  2. Innovation in the Sustainable Finance Space
  3. Increased Regulation Providing Additional Standardization
  4. Biodiversity and Natural Capital

### Latin America Sustainable Finance Team



#### Fanny Doucet

*Managing Director and Head, Sustainable Finance*

- Over 12 years of Capital Markets experience, including Canada & U.S. DCM and 4 years in Sustainable Finance; BComm from McGill University and CFA charter holder



#### Daniel Gracian

*Director, Sustainable Finance*

- Over 15 years of experience in Equity Research, Corporate Banking and Credit; MBA from INCAE Business School, Sustainable Finance Certificate from NYU



#### Dakota Mahar

*Associate, Sustainable Finance*

- Financial service experience in Retail Banking, Corporate Banking, Credit & Global Sustainability; BComm from the University of Alberta, GARP SCR certificate holder

# 2022 Trends and Year in Review

## MACRO LANDSCAPE

### Economic and Geopolitical Impacts on Sustainable Finance

After a record year in Sustainable Finance volumes in 2021, 2022 was about composure. High inflation across the Americas caused local debt markets to erode, slowing local Sustainable Finance volumes. This downward trend in ESG debt volumes was amplified by the rising rate environment central banks enacted to combat high inflation, coupled with repercussions stemming from the Ukraine-Russia conflict. Sustainable Finance in Latin America was also impacted by the local political environment, which experienced shifts in views across the region, impacting investor appetite when coupled with the global landscape. In 2022, we also saw investors reallocating capital out of emerging markets to developed nations in an attempt to minimize downside risk imminent from a deteriorating global economic environment.

### The Increasingly Problematic Climate Crisis

We saw an uptick in hydrometeorological hazards in 2022 due to the ever-growing climate crisis. Chile continued to experience drought that has lasted since 2010 and a worsening water scarcity crisis.<sup>1</sup> Extreme rainfall caused severe floods and mudslides in northeastern Brazil and Colombia. Peru and Mexico experienced 7.2 and 7.6 magnitude earthquakes respectively, and rising sea levels continued to engulf Mexican coastal regions.<sup>2</sup>

## SUSTAINABLE FINANCE LANDSCAPE

### Global Sustainability Market<sup>3</sup>

The Global Sustainable Finance market faced an inflection point in 2022 after a record year for ESG debt issuance in 2021. In 2022, volumes fell due to market volatility, with supply declining 14.2% year-over-year to approximately US\$1,490 billion. We also saw issuers with established programs leveraging sustainability labels to improve deal execution.

### Latin America Sustainability Market<sup>3</sup>

Latin America ESG debt volumes declined 38.2% in 2022 to approximately US\$36 billion, predominantly due to the aforementioned macro environment. Although several labelled debt products declined in volume, most evident in social bonds (-92.4% YoY), the silver lining was the increase in sustainability bonds (+32.5% YoY) and sustainability-linked loans (+14.5% YoY). Sovereigns, supranationals, and agencies maintained momentum in 2022, occupying the largest proportion of ESG transactions in Latin America with 26.3%. Chilean, Mexican, and Brazilian issuers drove ESG bond issuance in 2022, while Brazilian entities occupied the highest proportion of ESG loan volumes.

## INCREASED INNOVATION

### Enhanced Sovereign Sophistication

Innovation in the sovereign ESG space in 2022 was driven by Chile, who issued the world's first sovereign sustainability-linked bond, Uruguay, who issued the first sovereign sustainability-linked bond with a step-down mechanism, and Colombia, who published the first national green taxonomy in Latin America. The proportion of ESG bond issuance has also been growing for sovereigns, indicative of a growing desire for sustainability-related bonds compared to conventional options. Chile's ESG-related debt stock as a percentage of total is approximately 30%, a clear leader in the region.<sup>4</sup>






### Innovative Financing Solutions

In 2022, we saw an uptick in blue bonds issued in Latin America, demonstrating the market's increased focus on supporting marine and ocean-based projects. Furthermore, in 2022, the IFC, ICMA, UNGC, UNEP FI and ADB announced their commitment to develop guidelines that would provide market consistency and transparency in financing the blue economy. Blended finance continues to generate momentum, with renewables and green hydrogen being well-positioned for increased investment as a sector of focus.






### Changing Regulatory Environment<sup>5</sup>

Latin America saw new regulation in 2022, advancing ESG standards. Colombia's financial regulator SFC adopted the country's green taxonomy. Chile's new sustainability disclosure standards under Rule 461 took effect in December 2022. Brazil's ESG-related disclosure requirements under Resolution 59 fostered discussions prior to taking effect in January 2023. The Mexican government issued a resolution requiring public pension funds to incorporate ESG, with requirements set by CONSAR taking effect in January 2022.<sup>6</sup>

**Figure 1**  
CO<sub>2</sub> Emissions Per Capita in Latin America<sup>7</sup>

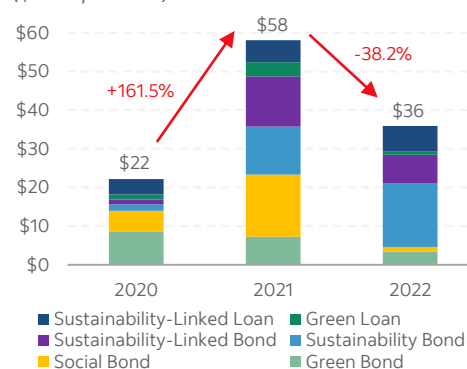
Country	CO <sub>2</sub> Emissions (tons per capita)	
	3.09	Global Average: 4.81
	1.64	
	4.61	
	1.53	
	2.28	

**Figure 2**  
Human Development and Social Progress Indices<sup>8,9</sup>

Country	HDI Rank*	SPI Rank**
	86 (High)	66 (Tier 3)
	84 (High)	67 (Tier 3)
	42 (Very High)	36 (Tier 2)
	88 (High)	70 (Tier 3)
	87 (High)	62 (Tier 3)

\* Human Development Index (HDI)  
\*\* Social Progress Index (SPI)

**Figure 3**  
LatAm Sustainable Debt Issuance  
(\$US eq. Billions)<sup>3</sup>



**Figure 4**  
NDC and Sustainability Frameworks<sup>10,11</sup>

Country	NDC Release	SBF/GBF*	SLBF**
	2022	✓	
	2020	✓	
	2020	✓	✓
	2020	✓	
	2022	✓	

\* Sustainable Bond Framework/Green Bond Framework  
\*\* Sustainability-Linked Bond Framework

# 2023 Sustainability Outlook

## MACRO OUTLOOK

### Economic, Geopolitical, and Climate Factors

With recession risks becoming more persistent, Scotiabank Economics is forecasting GDP growth across the PAC countries to shrink to 0.9%, with deceleration stemming from tightening monetary policy to combat high inflation.<sup>12</sup> However, central banks are expected to ease monetary policy in the second half of 2023 as inflation moderates. Increased tensions from geopolitical conflict and enhanced negative climate change-related impacts from extreme weather events could also affect the region during 2023.

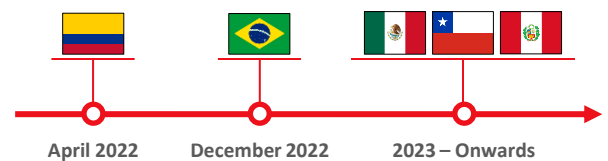
## KEY THEMES IN LATIN AMERICA SUSTAINABLE FINANCE IN 2023

### 1 Local Taxonomy Development

Colombia led the Latin America region in being the first country to release a green taxonomy, focused on providing clarity for investments in green projects and initiatives nationally. At the end of 2022, Brazil also established and released an ESG taxonomy of their own, covering sanitation and water infrastructure. In the next few years, we expect other nations in the Latin American region to launch local taxonomies, including Mexico, Chile, and Peru, which currently have taxonomies in development. Local taxonomies will be instrumental in progressing ESG in Latin America as they will bring more transparency to the market and more certainty to investors that they are putting funds towards sustainable economic activities.

Figure 1

Timeline of Latin America Taxonomy Development



### 2 Innovation in the Sustainable Finance Space

Latin American countries have continuously been pioneers in offering new sustainability financing products. We see additional products and structures gaining traction in 2023, including:

- **Blue Bonds:** Targeted at preserving oceans, marine ecosystems, fresh water use, and sanitation
- **New Product Combinations:** Green Sustainability-Linked Loans and Green Sustainability-Linked Bonds
- **New Financing Structures:** Sustainability-Linked Bonds with annual step-ups as well as step-downs
- **New Financing Products:** Blended finance, used to increase investments in emerging technologies

### 3 Increased Regulation Providing Additional Standardization

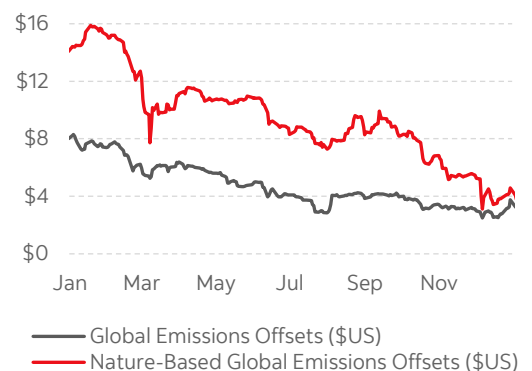
Strong regulation and standardization in Europe will continue to support increased ESG regulation in Latin America, especially in regards to disclosure and transparency. Governments in Latin America are realizing the risks associated with greenwashing on the back of increased scrutiny, and will be implementing standards to reduce potential reputational risks. In 2023, we will see the effectiveness of Chile and Brazil's new ESG-related disclosure requirements, which took effect in December 2022 and January 2023 respectively.<sup>5</sup> This increased regulation and standardization will in turn improve investor protection and sentiment, which could result in an uptick in ESG-related issuance in 2023. In 2023, the IFRS is expected to deliver their climate-related disclosure standard, after creating the ISSB in 2021 as a response to investor demands for high quality and consistent sustainability information.<sup>13</sup> After finalization of the standards, IOSCO will start its review and eventual recommendation to its 130 members, if ultimately endorsed.

### 4 Biodiversity and Natural Capital

COP27 advanced the sustainability narrative for Latin American countries, with 11 Latin American and Caribbean countries signing a joint statement on climate finance, cementing their commitment to ESG information access and climate policies.<sup>14</sup> COP15 is being described as a "Paris Moment" for biodiversity following the launch of Nature Action 100 and the Kunming-Montreal Global Biodiversity Framework, with the Taskforce for Nature-Related Financial Disclosures framework scheduled for September 2023. This is highly pertinent to Latin America, which is home to ~40% of species and ~25% of forests globally, as well as the world's second largest reef.<sup>15</sup> Latin American countries will benefit in 2023 from the accelerating carbon credit market, being the world's second largest provider of voluntary credits globally, with ~20% market share in 2020 and 2021.<sup>16</sup> Finally, we expect to see an uptick in financing structures incorporating biodiversity KPIs, and use of proceeds instruments tackling natural capital preservation.

Figure 2

Nature-Based and Global Emission Offsets<sup>3</sup>



# Endnotes and Abbreviations

## ENDNOTES

- <sup>1</sup> Nasa Earth Observatory: [A Strained Water System in Chile](#)
- <sup>2</sup> United States Geological Survey: [Peru Earthquake](#), [Mexico Earthquake](#)
- <sup>3</sup> Bloomberg Finance L.P., Scotiabank
- <sup>4</sup> Government of Chile Ministry of Finance: [ESG-Related Debt](#)
- <sup>5</sup> Fitch Ratings: [LatAm Regulatory Developments](#)
- <sup>6</sup> S&P Global: [Mexico ESG Pension Fund Requirements](#)
- <sup>7</sup> EDGAR: [Global CO<sub>2</sub> Emissions 2021](#)
- <sup>8</sup> UNDP: [Human Development Report 2021/2022](#)
- <sup>9</sup> Social Progress Imperative: [Social Progress Index 2022](#)
- <sup>10</sup> UNFCCC: [Nationally Determined Contributions Registry](#)
- <sup>11</sup> Country Filings: [Mexico SBF](#), [Chile SBF](#), [Chile SLB Framework](#), [Brazil SBF](#), [Peru SBF](#), [Colombia GBF](#)
- <sup>12</sup> GDP Forecast: [Scotiabank](#)
- <sup>13</sup> KPMG: [ISSB Developments](#)
- <sup>14</sup> United Nations: [Latin American and Caribbean Countries' Joint Statement](#)
- <sup>15</sup> Nature.org: [Latin America Biodiversity](#)
- <sup>16</sup> IETA: [Voluntary Carbon Markets in Latin America](#)

## ABBREVIATIONS

<b>ADB</b>	Asian Development Bank
<b>CON SAR</b>	Comisión Nacional del Sistema de Ahorro para el Retiro
<b>COP</b>	Conference of the Parties
<b>COP15</b>	Conference of the Parties, United Nations Convention on Biological Diversity
<b>COP27</b>	Conference of the Parties, United Nations Framework Convention on Climate Change
<b>EDGAR</b>	Emissions Database for Global Atmospheric Research
<b>ESG</b>	Environmental, Social, Governance
<b>GBF</b>	Green Bond Framework
<b>GDP</b>	Gross Domestic Product
<b>HDI</b>	Human Development Index
<b>ICMA</b>	International Capital Market Association
<b>IETA</b>	International Emissions Trading Association
<b>IFC</b>	International Finance Corporation
<b>IFRS</b>	International Financial Reporting Standards
<b>IOSCO</b>	International Organization of Securities Commissions
<b>ISSB</b>	International Sustainability Standards Board
<b>KPI</b>	Key Performance Indicator
<b>NDC</b>	Nationally Determined Contributions
<b>PAC</b>	Pacific Alliance
<b>SBF</b>	Sustainable Bond Framework
<b>SFC</b>	Superintendencia Financiera de Colombia
<b>SLB</b>	Sustainability-Linked Bond
<b>SLBF</b>	Sustainability-Linked Bond Framework
<b>SPI</b>	Social Progress Index
<b>UNDP</b>	United Nations Development Programme
<b>UNEP FI</b>	United Nations Environment Programme Finance Initiative
<b>UNFCCC</b>	United Nations Framework Convention on Climate Change

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